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TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1957

No. 97

UNITED STATES OF AMERICA, PETITIONER,

vs.

R. F. BALL CONSTRUCTION COMPANY, INC., AND UNITED PACIFIC INSURANCE COMPANY.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

Petition for certiorari filed April 4, 1957.

Certiorari granted May 13, 1957

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UNITED STATES DISTRICT COURT, WESTERN DISTRICT OF TEXAS
SAN ANTONIO DIVISION

Civil Action No. 1997

R. F. BALL CONSTRUCTION COMPANY, INC.,
Plaintiff,

vs.

MARCUS M. JACOBS AND HENRY LESKY, d/b/a MARCUS M. JACOBS CO., *et al.*,
Defendants.

Stipulation of Facts—Filed January 11, 1955

Solely for the purposes of this action, the undersigned parties hereby stipulate the following facts:

1. On June 26, 1951, R. F. Ball Construction Company, Inc. entered into a contract with the Housing Authority of the City of San Antonio, Texas for the construction of housing project TEX 6-10.

2. The Housing Authority of the City of San Antonio is an organization existing by virtue of Article 1269 (K), Texas R.C.S. (1925), as amended.

3. On July 17, 1951, R. F. Ball Construction Company, Inc. subcontracted the painting and decorating, taping and floating of sheetrock and waterproofing of masonry units on housing project TEX 6-10 to Marcus M. Jacobs and Henry Lesky, d/b/a Marcus M. Jacobs Company, 811 Capitol Avenue, Houston, Texas. As a part of the subcontract, Marcus M. Jacobs and Henry Lesky, d/b/a Marcus M. Jacobs Company agreed:

> • • • to furnish and pay for all labor, material, tools, equipment, compensation insurance and public liability and property damage insurance (carried in responsible companies and in limits satisfactory to R. F. Ball Construction Company, Inc.), also keep records and make payments on all Federal and/or State Payroll Taxes and/or deductions, together with all other incidentals necessary to complete in a good and workmanlike manner (the subcontracted work) • • •

4. On July 23, 1951, Marcus M. Jacobs and Henry Lesky, d/b/a Marcus M. Jacobs Company (as principals) and United Pacific Insurance Company (as surety) executed a bond in the amount of $229,029, with R. F. Ball Construction Company, Inc. as obligee, conditioned upon the faithful performance by the principals of the subcontract with respect to housing project TEX 6-10 (and also housing project TEX 6-7, not here material) "• • • according to its terms, covenants, and conditions • • •."

5. According to the terms of the subcontract, the subcontract price of $137,906 was payable in monthly installments of 90% of the value of the work completed, leaving a balance of 10% of the value of the completed work at all times unpaid, which balance was to be paid to Jacobs and Lesky upon the acceptance of the work of R. F. Ball Construction Company, Inc. by the Housing Authority of the City of San Antonio, Texas.

6. On October 1, 1951, the business of Marcus M. Jacobs and Henry Lesky, d/b/a Marcus M. Jacobs Company was incorporated under the name Marcus Jacobs Co., Inc. and the corporation succeeded to all rights of the partnership, in said contract by virtue of an assignment duly executed on said date.

7. On April 30, 1953, the Housing Authority of the City of San Antonio, Texas accepted the work of R. F. Ball Construction Company, Inc. and, thereafter, on October 8, 1953, since Marcus Jacobs Co., Inc. had performed the work required by the subcontract, it was agreed by the R. F. Ball Construction Company, Inc. and Marcus Jacobs Co., Inc. that the sum of $13,228.55 (representing retained percentages according to the terms of the subcontract) be-

came due and owing to Marcus Jacobs Co., Inc. as of April 30, 1953.

8. The following table sets forth the pertinent information with respect to the federal tax liabilities of Marcus Jacobs Co., Inc.:

Kind of Tax	Taxable Period	Date Assessment List Received By District Director	Date of Notice and Demand
W-H	4 Q. '52	3-16-53	3-19-53
FUTA	1952	5-14-53	5-18-53
FICA	1 Q. '53	5-15-53	5-15-53

Date Notice of Tax Liens Filed Harris Cty.	Amount Assessed	Outstanding Balance
6- 9-53	$11,174.53	$ 6,343.24
9- 5-53	1,012.47	1,012.47
5-18-53	9,655.14	9,655.14
	$21,842.14	$17,010.85

The parties make no stipulation as to whether or not these taxes arose in connection with the performance of the subcontract referred to in paragraph 3.

9. Herweck Co., Inc. furnished paint and other materials to Marcus Jacobs Co., Inc. in connection with the performance of the subcontract, as a result of which it has claim against Marcus Jacobs Co., Inc. for $981.83. Herweck Co., Inc. notified United Pacific Insurance Company, the Housing Authority of the City of San Antonio, Texas, and R. F. Ball Construction Company, Inc. of its claim on July 13, 1953. No stipulation is made as to the adequacy of any notices of claim to hold United Pacific Insurance Company liable on its bond.

10. S. H. Kottwitz, d/b/a S. H. Kottwitz & Company, furnished compensation and public liability insurance to Marcus Jacobs Co., Inc., as a result of which he has a claim against Marcus Jacobs Co., Inc. for $2,431.05 for insurance premiums due on November 1, 1952. S. H. Kottwitz notified R. F. Ball Construction Company, Inc. and

United Pacific Insurance Company of his claim on September 18, 1953.

11. This case originated in the State District Court of Bexar County, plaintiff therein filing a suit in the nature of a Bill of Interpleader, and tendering into court the $13,228.55. The allegations of plaintiff's petition with reference to the dispute over such fund and with reference to its inability to make payment thereof without subjecting itself to possible double liability, are true. Plaintiff asks allowance of interpleader fee and its court costs, to be payable out of the $13,228.55. It is stipulated that a reasonable fee for the services performed by Simon & Simon, attorneys for R. F. Ball Construction Co., Inc. (the interpleader) is $500; provided a fee may be allowed by the Court to the interpleader's attorneys out of the $13,228.55 in question, under applicable principles of law.

(s) RICHARD W. SIMON
For R. F. Ball Construction Company, Inc.

(s) JOSH H. GROCE
For United Pacific Insurance Company

(s) PATRICK H. SWEARINGEN, JR.
For The Herweck Co., Inc.

(s) ALLEN H. KOTTWITZ
For S. H. Kottwitz & Company

(s) C. H. HERRING
United States Attorney

Dated: 1-11-55.

Filed: 1-11-55.

IN UNITED STATES DISTRICT COURT

Stipulation of Facts—Filed January 17, 1955

Solely for the purpose of this action, the undersigned parties hereby stipulate to the following facts:

That on the 21st day of July, 1951, Marcus M. Jacobs and Henry Lesky, d/b/a Marcus M. Jacobs Company, applied to United Pacific Insurance Company for a faithful performance bond payable to R. F. Ball Construction Com-

pany in the penal sum of $229,029.00, which bond was thereafter duly executed by said company. In the application for said bond it was provided in part as follows:

> "the undersigned does by these presents assign, transfer and convey to United Pacific Insurance Company, the Company, as of this date, as collateral security for the full performance of the covenants and agreements herein contained and the payment of any other indebtedness or liability of the undersigned to the Company, whether heretofore or hereafter incurred the following:
>
> • • • • • • • •
>
> "(d) All right, title and interest of the undersigned in and to and all percentages retained by the Obligee under said contract, and any and all estimates, payments extra, final payments, and other sums that .... may be due or may thereafter become due under said contract to or on behalf of the undersigned."

That said application likewise contained the following provision:

> "The agreements and covenants herein contained shall be binding upon the undersigned, both jointly and severally, and upon their heirs, personal representatives, successors and assigns of each, jointly and severally. ..."

That, as has been previously stipulated on October 1, 1951, the business of Marcus M. Jacobs and Henry Lesky, d/b/a Marcus M. Jacobs Company, was incorporated under the name of Marcus M. Jacobs Company, Inc. and the Corporation succeeded to all rights and liabilities of the partnership in said contract by virtue of an assignment duly executed on said date.

Thereafter, said Marcus M. Jacobs Company, Inc. applied to United Pacific Insurance Company for a bond payable to Darby Construction Company and the Perkins Construction Company in the sum of $35,591.00 covering a sub-contract in Louisville, Kentucky, which bond was duly executed by said Company. That in the application for said bond, dated April 4, 1952, the said Marcus M. Jacobs Company, Inc., agreed "to indemnify and keep indemnified,"

the Company against all loss, costs, damages, expenses and attorneys' fees whatever".

Thereafter, between December of 1953 and March of 1954, by virtue of its obligations under said bond said United Pacific Insurance Company was required to make payments as follows:

Kelley-Mahone Company	$ 4,569.17
Derby Construction Co., Inc. and the Perkins Construction Co. and B. L. Shamburger	7,000.00
John M. Hennessy, Clerk	14.45
Edward H. Marcus Paint Co.	37.46
Fulbright, Crooker, Freeman & Bates, Attys	398.12
Boehl, Stopher, Kilgarrif, Graves & Deindoerfer, Attorneys	952.68
Total	$12,971.88

Dated:

UNITED PACIFIC INSURANCE COMPANY
(s) JOSH H. GROCE
United States Attorney
(s) CHARLES F. HERRING

Filed: January 17, 1955.

IN UNITED STATES DISTRICT COURT

Memorandum Opinion—February 6, 1956

The Court, having considered the pleadings, the stipulated facts, and the briefs and oral arguments of the parties in the above cause, finds the facts and the law to be in favor of R. F. Ball Construction Company, Inc., and United Pacific Insurance Company.

The Clerk will advise counsel for all parties of the opinion of the Court and request counsel for United Pacific Insurance Company to prepare and submit to the Court tentative findings of facts and conclusions of law and judgment, and furnish copies thereof to cousel for all other parties.

(s) BEN H. RICE, JR.
United States District Judge

February 6, 1956.
Filed: February 7, 1956.

IN UNITED STATES DISTRICT COURT

Memorandum of Decision—April 17, 1956

Pursuant to Rule 52(a) this Memorandum of Decision is filed and contains findings of fact and conclusions of law in this case, the facts of which have all been stipulated by the parties.

On June 26, 1951, R. F. Ball Construction Company (hereinafter called Ball) entered into a contract with the Housing Authority of the City of San Antonio (hereinafter called Housing Authority) for the construction of a housing project. Shortly thereafter Ball subcontracted the painting and decorating involved in such contract to Marcus M. Jacobs Company, a co-partnership consisting of Marcus Jacobs and Henry Leskey (hereinafter called Jacobs) for the sum of approximately $230,000.00 and required of it a faithful performance bond. On July 21, 1951, Jacobs applied to United Pacific Insurance Company (hereinafter called Bonding Company) for such performance bond, and one of the considerations agreed to in the application for such bond was an unconditional assignment by Jacobs to the Bonding Company of all percentages retained by Ball under the Jacobs sub-contract as collateral security for the protection of the Bonding Company, not only for losses growing out of the Housing job, but for the "payment of any other indebtedness or liability" of Jacobs to the Bonding Company, "whether heretofore or hereafter incurred". A few months thereafter the business of Jacobs was incorporated into Marcus M. Jacobs Company, Inc. (hereinafter called Jacobs, Inc.) and the corporation succeeded to all rights and liabilities of the partnership. No party to this controversy has raised any question about the succession, so this mutation from the partnership to the corporation is immaterial and will not be referred to further. See *Mites* v. *Aetna*, 1 F. Supp. 925; *Illinois Surety Co.* v. *Davis*, 244 U.S. 376, 37 S.Ct. 614, 61 L.Ed. 1202.

Thereafter, on April 4, 1952, Jacobs, Inc. obtained from the Bonding Company a similar bond on another sub-contract in Louisville, Kentucky, in the application for which Jacobs, Inc. agreed "to indemnify and keep indemnified the company against all loss, costs, damages, expenses and attorney's fees whatsoever * * *", and under such bond the

Bonding Company exposed itself to a liability of some $35,000.00.

On April 30, 1953, the Housing Authority accepted the work of Ball and subsequently it was agreed between Ball and Jacobs, Inc. that the sum of $13,228.55 representing the retained percentages according to the terms of the subcontract, was due and owing on this job by Ball to Jacobs, Inc., as of April 30, 1953.

In May, June and September of 1953, and long after the assignment as collateral security of the retained percentages on the Housing Authority job had been made to the Bonding Company, and long after the Bonding Company had executed its obligation under its bond on the Louisville job, the United States Government filed tax liens against Jacobs, Inc. totalling $17,010.85. No stipulation is made by the parties that this tax claim arose out of Jacobs, Inc.'s failure to pay taxes incurred on either the Housing Authority job or the Louisville job, so that this court must assume that they are ordinary tax liens, not growing out of the particular jobs in question, and the Government here makes no claim on either of the bonds.

After the tax liens had been filed, the potential liability on the Kentucky job incurred by the Bonding Company on April 4, 1952, became an actual liability and the Bonding Company was required to pay, by virtue of its bond in connection with the Kentucky project, the sum of $12,971.88.

Thereafter, because of numerous conflicting claims presented to Ball, Ball was unable to determine with safety to itself to whom the $13,228.55 of retained percentages which it held in its hands should be paid. Therefore, Ball filed this suit, which is an interpleader action, making as parties defendant Jacobs and Jacobs, Inc., the Government, the bonding Company and certain suppliers of materials and services on the Housing Authority job, and asking for an interpleader's fee of $500.00, which has been stipulated to be a reasonable fee if under the law any interpleader's fee is payable. The Government filed its answer claiming the funds by virtue of its tax liens; the Bonding Company filed its answer claiming $12,971.88 of the funds by virtue of its assignment as collateral security and the loss which it sustained on the Kentucky job; the Herweck Company, Inc. filed its claim for $981.83 for materials

furnished on the Housing job; S. H. Kottwitz & Company filed its claim for compensation and public liability insurance premiums on said job of $2,431.05. Several other claimants were made parties defendant but failed to answer and make claim, and default judgment was rendered against them. Kottwitz, although filing a claim, has not appeared in any of the hearings, and has failed to file any briefs herein in support of his claim; and it appearing to the court that under decision such as *U.S.* v. *Yates*, 204 S.W.2d 399, as well as by virtue of default, Kottwitz is not entitled to recover, judgment will go against him.

The Herweck Company has filed its brief contending that it is entitled to priority, but has likewise stated that the Bonding Company had agreed to satisfy its claim if the Bonding Company prevailed herein, and has asked, therefore, that judgment go in favor of the Bonding Company, and in view of this Herweck likewise goes out of the case, under the court's rulings, since the court is of the opinion that the Bonding Company should prevail herein, and will respect the agreement between Herweck and the Bonding Company.

The principal question for determination by this court is as to which lien is prior—the Government's tax lien which arose by virtue of the filing of the notice of its tax liens in May, June and September of 1953, or the contract lien of the Bonding Company which arose long prior thereto by virtue of the assignment of the retained percentages in question by Jacobs to the Bonding Company, which by contract protected the Bonding Company from the loss which it incurred on the Louisville job, which became a potential loss upon the execution of the Louisville bond on April 4, 1952, prior to the filing of the Government's tax liens, but which was not paid under its bond until after the filing of the Government's tax liens.

The Government cites and contends that the case of *U.S.* v. *Security Trust & Savings Bank*, 340 U.S. 47, 71 S.Ct. 111; *U.S.* v. *Gilbert Associates*, 345 U.S. 361, 73 S.Ct. 701; *U.S.* v. *City of New Britain*, 347 U.S. 81, 74 S.Ct. 367; *U.S.* v. *Acri*, 348 U.S. 211, 75 S.Ct. 239; *U.S.* v. *Liverpool, etc. Ins. Co.*, 348 U.S. 215, 75 S.Ct. 247; and *U.S.* v. *Scovil*, 348 U.S. 218, 75 S.Ct. 244, are in point and are controlling in this case, and says:

"* * * the principles of United States v. Security Trust & Sav. Bk.; United States v. New Britain; United States v. Scovil; United States v. Acri; and United States v. Liverpool & London Ins. Co. supra, must be applied."

The Bonding Company, on the other hand, contends that none of the liens in the above cited cases were contractual liens and that none of those cases dealt with mortgagees, pledgees, or purchasers within the meaning of Section 3672 of the Internal Revenue Code (now Sec. 6323, Title 26 U.S.C.), and further contends that in those cases the court was construing only the term "judgment creditor" and liens other than mortgages and pledges, and therefore says that such cases are not controlling in this case.

Section 3672 of the Internal Revenue Code provides in effect that filing of a federal tax lien does not affect the rights of any prior "mortgagee, pledgee, purchaser or judgment creditor". Most of the decisions of the Supreme Court cited above and referred to by the Government dealt with inchoate judgment liens and none of those cases dealt with the contract lien of a "mortgagee", "pledgee" or "purchaser". The latter three categories are all based upon a contract right of some sort, whereas the term "judgment creditor" and the other liens dealt with in those cases, such as water rent liens, municipal tax liens and landlord's distress liens, arose by virtue of some statutory right, not specifically referred to in Section 3672.

The Bonding Company contends that since its assignment as collateral security was based upon a contract which was prior in time to the Government's tax liens, it is either a mortgagee, pledgee or purchaser of the retained funds and it disclaims any contention on its part that it is a judgment creditor, or claims to be anything other than a mortgagee, pledgee or purchaser.

In the case of *National Refining Co.* v. *U.S.*, 106 F.2d 951, the taxpayer was indebted to National Refining Company, which took an assignment as collateral security from the taxpayer of certain commissions to be earned by him under his contract with the Government "when they should become available to him". Before any money had been earned or paid under this assignment, the Government perfected a tax lien and there claimed that the assignment

as collateral security was subordinate. In holding that the assignment to the National Refining Company took priority over the Government's tax claim, the court said:

> "We think it safe to say that one who for a valuable present consideration acquires a property or interest in property, is 'a purchaser' within the meaning of 26 U.S.C.A. Internal Revenue Code, Section 3672."

It cannot be doubted that the execution by the Bonding Company of the bonds in this instance constituted "a valuable present consideration" and it further cannot be doubted that at the time of the assignment as collateral security of the retained percentages by Jacobs to the Bonding Company, the Bonding Company acquired an interest in these retained percentages. However, I do not rest my decision on this ground since in the *Scovil* case the Supreme Court said: "A purchaser within the meaning of Sec. 3672 usually means one who acquires title for a valuable consideration in the manner of vendor and vendee".

In the case of *Knight* v. *Knight*, 71 N.Y. Supp. 2d 357, the Government claimed that its lien for federal taxes was superior to a prior assignment of future wages as collateral security for payments to the taxpayer's divorced wife. The court there held:

> "The Government attempts to avoid the impact of Section 3672 by contending that respondent is not a pledgee. We think that as the assignment of wages made by defendant Knight was as security for, and a means of payment of, the defendant's principal obligation to pay plaintiff $20,000.00, the plaintiff comes within the classification of a pledgee."

This case was subsequently affirmed by the Court of Appeals, 80 N.E. 2d 344, and was not appealed by the Government to the Supreme Court of the United States.

The assignment of retained percentages in the case at bar was made by Jacobs as security for and a means of payment of Jacob's obligation to indemnify the Bonding Company against loss, and it could be said therefore, as was held in the *Knight* case, that the Bonding Company "comes within the classification of a pledgee."

In my opinion, however, the Bonding Company in this instance more nearly comes within the classification of a "mortgagee" under the Texas law, which "should be given considerable weight in determining whether or not" the Bonding Company is a mortgagee. See *U.S.* v. *Gargill*, 218 F.2d 556 at 560. According to 29 Tex. Jur. 786,

> "A mortgage, in the broadest sense of the term is a pledge of property, either real or personal, or of a chose in action, as security for the performance of an obligation."

According to 29 Tex. Jur. 838,

> "A mortgage which purports to secure future debts is not ineffectual or invalid. On the contrary the lien created will be enforced not only in a dispute between the mortgagor and mortgagee but also in a controversy involving the rights of one who claims under the mortgagor."

As was recently stated by the Supreme Court of Iowa in *Evans* v. *Stewart*, 66 N.W. 2d 442 at 449:

> "We feel the requirement that the lienholder be a 'mortgagee' is a requirement of status—that he be in the position of one holding a mortgage".

It is true that the parties to the assignment as collateral security in this instance did not place a label on this transaction as either a mortgage, a pledge or a purchase, but courts do not decide cases on nomenclature; they look to the substance of the transaction; and the substance of the assignment here was to put the Bonding Company in the status of either a mortgagee, pledgee or purchaser, and therefore Section 3672 applies.

In *Northern Nat. Bank* v. *Northern Minn. Nat. Bank*, 70 N.W. 2d 118, the Supreme Court of Minnesota held that an assignment as security of retained percentages under a construction contract to a bank which was prior in time to a Federal tax lien, was superior to the claim of the Government, which is precisely the situation here. The Government did not appeal that case to the Supreme Court of the United States.

The distinction between a contract lien and a statutory lien is made clear by comparing the case of *Evans* v. *Stewart*, supra, with the *Scovil* case, supra. In the *Scovil* case, the Supreme Court held that prior to the time it ripened into a final judgment, an incompleted statutory, landlord's lien was inferior to a federal tax lien, since the holder thereof was neither a "mortgagee", "pledgee", "purchaser" nor "judgment creditor". In the *Evans* case, the court held that a written contract landlord's lien contained in the lease was superior to a federal tax lien because it was a "mortgage" within 3672. The Government did not appeal the *Evans* case.

The Government argues that if an attachment or other judicial lien is not sufficiently "choate" or complete "to defeat a subsequent tax lien" then a mortgage to secure future indebtedness should likewise be inferior to a subsequent tax lien. Congress has in effect stated in Sec. 3672 that before an attaching, or other similar statutory lien or, could claim priority over the Government, his claim had to ripen into a final judgment. *U.S.* v. *Security Trust, etc.*, supra. *U.S.* v. *Acri*, supra. No such qualification was placed by Congress on the contractual lien of a "mortgagee". It is the Congress which enacts the law with refence to priorities and not the courts, and I therefore hold that the Bonding Company under its assignment as collateral security, became a "mortgagee" within the meaning of 3672 and was, therefore, not affected by the tax liens which were subsequent in time.

While admitting that "the Government does not claim the status of an innocent purchaser for value", the Government does contend that because the Bonding Company did not record its assignment under the provisions of Article 260-1, R.C.S. of Texas, said assignment is therefore inferior to the claim of the Government. In Texas, the recording of an assignment adds nothing to the validity thereof as between the parties. (9 Tex. Jur. 97).

As I see it, the Government is seeking to read into Section 6372 provisions which Congress has not seen fit to insert therein and the Government would have this court construe such section to read:

> "Such lien shall not be valid as against any mortgagee *whose mortgage is due at a certain time and in a cer-*

tain amount and which mortgage has been duly recorded in accordance with law."

Had Congress seen fit to make such a requirement it could have done so, but I decline to read these words into the statute, and on this point I concur in the opinion of Judge Wyche in the case of *U.S.* v. *Anders Contracting Company*, 111 F.Supp. 700, where the Government made identically this same contention, was overruled, and did not appeal.

There remains for consideration the question as to whether or not Ball is entitled to any interpleader's fee in this case. The Bonding Company has raised no objection to awarding such fee and in fact has presented cogent arguments as to why such fee should be allowed. The Government, on the other hand, contends that under the case of *U.S.* v. *Liverpool, etc.*, supra, the interpleader is not entitled to his costs. There can be no question as to the status of Ball in this matter. Ball was an innocent stakeholder confronted with conflicting claims to a fund which was in his hands, and he adopted the proper course of employing attorneys and tendering this money into court. As was said by the Supreme Court in its opinion therein, the *Liverpool* case had to do solely with a garnishee's fee under Rule 677 of the Texas Rules of Civil Procedure and did not purport to deal with an Interpleader action under Texas Rule 43 or Rule 22 of the Federal Rules of Civil Procedure, and it is therefore not controlling. On the other hand, the case of *U.S.* v. *Ullman*, 115 F.Supp. 211, is directly in point, and I adopt the reasoning of the court in that case and hold that Ball is entitled to his interpleader's fee in this case, and the remainder of the interpleaded fund, less costs, should be awarded to the Bonding Company.

The attorneys for the Bonding Company are directed to submit a judgment not inconsistent with this Memorandum.

Done on this 29th day of March, A.D. 1956.

(s) Ben H. Rice, Jr.
Chief Judge,
United States District Court,
Western District of Texas.

Filed: April 17, 1956.

IN UNITED STATES DISTRICT COURT

Findings of Fact and Conclusions of Law—April 17, 1956

FINDINGS OF FACT

1. On June 26, 1951, R. F. Ball Construction Company, Inc. (hereinafter referred to as Ball) entered into a contract with the Housing Authority of the City of San Antonio, Texas, for the construction of Housing Project TEX 6-10.

2. On July 17, 1951, Ball subcontracted the painting and decorating, taping and floating of sheetrock and waterproofing of masonry units on the Housing Project to Marcus M. Jacobs and Henry Lesky, d/b/a Marcus M. Jacobs Co.

3. As a part of the subcontract, Jacobs and Lesky agreed:

> * * * to furnish and pay for all labor, material, tools, equipment, compensation insurance and public liability and property damage insurance (carried in responsible companies and in limits satisfactory to R. F. Ball Construction Company, Inc.), also keep records and make payments on all Federal and/or State Payroll Taxes and/or deductions, together with all other incidentals necessary to complete in a good and workmanlike manner (the subcontracted work) * * *

4. On July 21, 1951, Jacobs and Lesky applied to United Pacific Insurance Company for a faithful performance bond, payable to Ball, in the penal sum of $229,029. The application contained the following clause:

> the undersigned does by these presents assign, transfer and convey to United Pacific Insurance Company, the Company, as of this date, as collateral security for the full performance of the covenants and agreements herein contained and the payment of any other indebtedness or liability of the undersigned to the Company, whether heretofore or hereafter incurred the following:
>
> * * * * * * * *
>
> (d) All right, title and interest of the undersigned in and to and all percentages retained by the Obligee under said contract, and any and all estimates, payments, extras, final payments, and other sums that

. . . . may be due or may thereafter become due under said contract to or on behalf of the undersigned.

5. On July 23, 1951, Jacobs and Lesky (as principals) and United Pecific (as surety) executed a bond in the amount of $229,029, with Ball as obligee, conditioned upon the faithful performance of the Housing Project subcontract "according to its terms, covenants, and conditions".

6. Under the terms of the subcontract, Ball was to retain 10% of the value of the completed work at all times until Ball's work had been accepted by the Housing Authority, at which time the 10% retained fund would be paid to Jacobs and Lesky.

7. On October 1, 1951, Jacobs and Lesky incorporated their business under the name of Marcus M. Jacobs Company, Inc. and the corporation succeeded to all of the partnership's rights in the Housing Project subcontract. Jacobs' and Lesky's contractual obligations under the application for the performance bond were binding upon their successors and assigns, which includes the corporation.

8. On April 4, 1952, Marcus M. Jacobs Company, Inc. applied to United Pacific Insurance Company for a bond in the amount of $35,591 payable to the Darby and Perkins Construction Companies covering a subcontract in Louisville, Kentucky. In this application, the corporation agreed to indemnify United Pacific against all loss (including expenses and attorneys' fees) which might be incurred as a result of writing the bond.

9. Pursuant to the application, United Pacific (as surety) and the corporation (as principal) executed a bond and, between December of 1953 and March of 1954, United Pacific, as surety under the bond, was required to make payments totaling $12,971.88.

10. On April 30, 1953, the Housing Authority accepted Ball's work and, pursuant to the subcontract, $13,228.55 (representing the 10% retained by Ball) became due and owing to Marcus Jacobs Company, Inc.

11. The following table sets forth the pertinent information with respect to Marcus Jacobs Company, Inc.'s tax liabilities to the United States:

Kind of Tax	Taxable Period	Date Assessment List Received by District Director
W-H	4 Q. '52	3/16/53
FUTA	1952	5/14/53
FICA	1 Q. '53	5/15/53

Date Notice of Tax Liens Filed	Outstanding Balance
6/ 9/53	$ 6,343.24
9/ 5/53	1,012.47
5/18/53	9,655.14
	$17,010.85

12. On July 13, 1953, Herweck Company, Inc. notified United Pacific, the Housing Authority, and Ball that it had a claim against Marcus Jacobs Company, Inc. for $981.83 as a result of paint and other materials furnished in connection with the performance of the subcontract.

13. On September 18, 1953, S. H. Kottwitz & Company notified Ball and United Pacific that it had a claim against Marcus Jacobs Company, Inc. for unpaid insurance premiums in the amount of $2,431.05.

14. On May 24, 1954, Ball commenced this action as an interpleader suit, tendering the $13,228.55 which it owed to Marcus Jacobs Co., Inc. into the registry of the District Court of Bexar County, Texas, asking interpleader's attorneys' fees and costs, to be paid out of the fund. It is agreed between the parties that, if Ball is entitled to receive an interpleader's attorneys' fee as a matter of law, a reasonable sum would be $500.

15. The following parties were named defendants:

Marcus M. Jacobs and Henry Lesky, individually and as partners, d/b/a Marcus M. Jacobs Co.
Marcus M. Jacobs Co., Inc.
United Pacific Insurance Company
Herweck Company, Inc.
Otto Dukes, d/b/a Otto Dukes Machinery Company

Floor Maintenance Bureau Products Company (a corporation)
J. T. Dulaney and R. T. Dulaney, partners, d/b/a Dulaney Service Company
S. H. Kottwitz & Company
The United States of America
R. L. Phinney, District Director of Internal Revenue.

16. The United States of America removed the case to this Court on June 15, 1954, and the $13,228.55 deposited by Ball in the registry of the State Court is now in the registry of this Court.

17. R. L. Phinney, District Director of Internal Revenue, was dismissed as a party.

18. On October 21, 1954, default judgments were entered against the following parties:

Marcus M. Jacobs and Henry Lesky, individually and as partners, d/b/a Marcus M. Jacobs Co.
Marcus Jacobs Co., Inc.
Otto Dukes, d/b/a Otto Dukes Machinery Company
Floor Maintenance Bureau Products Company (a corporation)
J. T. Dulaney and R. T. Dulaney, partners, d/b/a Dulaney Service Company.

19. The remaining parties (Ball, United Pacific, Herweck, Kottwitz, and the United States) submitted the case on a stipulation of facts.

20. The Court must decide what are the relative priorities of the following creditors with respect to the $13,228.55 now on deposit in the registry of this Court representing the retained fund owed by Ball to Marcus Jacobs Co., Inc. as a result of performance of the subcontract on the TEX 6-10 Housing Project:

(a) The United States of America (claiming under tax liens against all property and rights to property belonging to Marcus Jacobs Co., Inc.).

(b) United Pacific Insurance Company (claiming reimbursement for losses sustained as a result of the Louisville bond as assignee of the retained fund earned by Marcus Jacobs Co., Inc. in performing the TEX 6-10 Housing Project subcontract).

(c) Herweck Company, Inc. (an unpaid material man).

(d) S. H. Kottwitz & Company (holding a claim for unpaid insurance premiums).

(e) R. F. Ball Construction Company, Inc. (claiming interpleader's attorneys' fees).

Conclusions of Law

1. Herweck Company, Inc. has not shown that it has any lien on the retained fund in question, as such. Therefore, the claim of Herweck Company, Inc. will be considered an unsecured claim so far as this fund is concerned.

2. S. H. Kottwitz & Company has not shown that it has any lien on the retained fund in question. Therefore, the claim of S. H. Kottwitz & Company will be considered an unsecured claim so far as this fund is concerned.

3. R. F. Ball Construction Company, Inc., under the usual rule, is entitled to interpleader's attorneys' fees out of the fund in question and the parties have stipulated that a reasonable fee in this case is $500. Ball's right to this fee is superior to the tax liens asserted by the United States and to the claim of United Pacific Insurance Company and, therefore, Ball is entitled to receive $500 out of the $13,228.55 now on deposit in the registry of the Court.

4. As between the tax liens asserted by the United States and the assignment claimed by United Pacific Insurance Company, the assignment gave United Pacific an interest in the retained fund which is superior to the Government's tax liens. United Pacific's claim totals $12,971.88 plus expenses and attorneys' fees in connection with the loss sustained under the Louisville bond. United Pacific is therefore entitled to receive the balance of the $13,228.55 on deposit in the registry of the Court after the payment of $500 to Ball and costs.

Done at the request of the government on this 14th day of April, 1956.

(s) Ben H. Rice, Jr.
Chief Judge,
United States District Court,
Western District of Texas.

Filed: April 17, 1956.

IN UNITED STATES DISTRICT COURT

Final Judgment—April 17, 1956

[Title omitted]

On the 17th day of April, 1956, the above case having heretofore been taken under advisement by the court, and the court having rendered his opinion herein in favor of R. F. Ball Construction Company and United Pacific Insurance Company, the following final judgment is rendered in this cause:

The default judgments heretofore rendered against Otto Dukes, d/b/a Otto Dukes Machinery Company, Floor Maintenance Bureau Products Company (a corporation), J. T. Dulaney and R. T. Dulaney, partners, d/b/a Dulaney Service Company, are hereby made final.

Judgment is here rendered against S. H. Kottwitz & Company and Herweck Company, Inc.

Judgment is here rendered in favor of R. F. Ball Construction Company in the sum of $500.00 as its attorney's fees, and the Clerk of the court is directed to pay said sum of $500.00 out of the funds in the registry of this court direct to R. F. Ball Construction Company.

The Clerk is likewise directed to reimburse himself for all costs of suit herein.

The remainder of the funds in the hands of the Clerk being less than the amount of the claim of the United Pacific Insurance Company, the Clerk is directed to pay the remainder of the funds involved in this suit which are in the registry of the court direct to United Pacific Insurance Company.

It is the further order of this court that the United States take nothing by this suit.

DONE AND ORDERED ENTERED on this, the 17th day of April, 1956.

(s) BEN H. RICE, JR.
Judge.

Entered: Civil Order Book, Vol. No. 7, Page 365.

Filed: April 17, 1956.

IN UNITED STATES DISTRICT COURT

Notice of Appeal to Court of Appeals Under Rule 73(b)—June 15, 1956

Notice is hereby given that defendant in the above entitled and numbered cause hereby appeals to the United States Court of Appeals for the Fifth Circuit from the final judgment entered in this action on April 17, 1956.

(s) RUSSELL B. WINE,
United States Attorney
Western District of Texas.

Filed: June 15, 1956.

IN UNITED STATES DISTRICT COURT

Statement of Points to Be Relied Upon on Appeal—July 12, 1956

Pursuant to Rule 75(d) of the Federal Rules of Civil Procedure, the United States of America, appellant, hereby makes the following statement of the points upon which it intends to rely on appeal:

(1) The Court erred in concluding that R. F. Ball Construction Company, Inc., was entitled to receive an interpleader's attorneys' fee out of the $13,228.55 on deposit in the registry of the Court in preference to the claim of the United States to that fund in its entirety;

(2) The Court erred in concluding that United Pacific Insurance Company's assignment gave United Pacific an interest in the $13,228.55 retained fund which is superior to the Government's tax liens;

(3) The Court erred in ordering the payment of $500 on R. F. Ball Construction Company, Inc., out of the $13,228.55 on deposit in the registry of the Court and in ordering the balance of that fund, less costs of suit, to be paid to United Pacific Insurance Company;

(4) The Court erred in ordering that the United States take nothing in this suit.

(s) RUSSELL B. WINE,
United States Attorney

Dated: July 12, 1956.
Filed: July 12, 1956.

IN UNITED STATES DISTRICT COURT

Designation of Contents of Record on Appeal—

July 12, 1956

Pursuant to Rule 75(a) of the Federal Rules of Civil Procedure, the United States of America, appellant, hereby designates the following portions of the record, proceedings, and evidence to be contained in the record on appeal:

(1) Stipulation of Facts filed January 14, 1955;

(2) Supplemental Stipulation of Facts filed January 17, 1955;

(3) Memorandum Opinion entered February 6, 1956;

(4) Memorandum of Decision entered March 29, 1956;

(5) Findings of Fact and Conclusions of Law entered April 14, 1956;

(6) Judgment entered April 17, 1956;

(7) Notice of Appeal filed by appellant on June 15, 1956;

(8) Appellant's Statement of Points to be Relied Upon On Appeal.

(s) RUSSELL B. WINE,
United States Attorney

Dated: July 12, 1956.

Filed: July 12, 1956.

Clerk's Certificate to foregoing Transcript (omitted in printing).

IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

Argument and Submission—November 20, 1956 (omitted in printing).

IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 16276

UNITED STATES OF AMERICA,

Appellant,

VERSUS

R. F. BALL CONSTRUCTION COMPANY, INC.,
and
UNITED PACIFIC INSURANCE COMPANY,

Appellees.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF TEXAS

Opinion—December 26, 1956

Before CAMERON, JONES and BROWN, Circuit Judges.

Per Curiam: The facts of this case are well recited and the controlling principles of law are well stated in the opinion of Judge Rice, *R. F. Ball Construction Company* v. *Jacobs*, 140 F. Supp. 60. For the reasons there set forth the judgment appealed from is

AFFIRMED.

IN THE UNITED STATES COURT OF APPEALS

No. 16276

UNITED STATES OF AMERICA,

VERSUS

R. F. BALL CONSTRUCTION COMPANY, INC., and UNITED PACIFIC INSURANCE COMPANY.

Judgment—December 26, 1956

This cause came on to be heard on the transcript of the record from the United States District Court for the Western District of Texas, and was argued by counsel;

On consideration whereof, It is now here ordered and adjudged by this Court that the judgment of the said District Court appealed from in this cause be, and the same is hereby, affirmed.

Clerk's Certificate to foregoing Transcript (omitted in printing).

SUPREME COURT OF THE UNITED STATES

[Title omitted]

Order Extending Time to File Petition for Writ of Certiorari

UPON CONSIDERATION of the application of counsel for petitioner,

IT IS ORDERED that the time for filing petition for writ of certiorari in the above-entitled cause be, and the same is hereby, extended to and including April 5th, 1957.

HUGO L. BLACK,
Associate Justice of the Supreme Court of the United States.

Dated this 21st day of March, 1957.

SUPREME COURT OF THE UNITED STATES

Order Allowing Certiorari—Filed May 13, 1957

The petition herein for a writ of certiorari to the United States Court of Appeals for the Fifth Circuit is granted, and the case is transferred to the summary calendar.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

☆ U. S. GOVERNMENT PRINTING OFFICE 1957—439304/P.O. 180

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In the Supreme Court of the United States

OCTOBER TERM, 1956

No. ---

UNITED STATES OF AMERICA, PETITIONER

v.

R. F. BALL CONSTRUCTION COMPANY, INC., AND UNITED PACIFIC INSURANCE COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The Solicitor General, on behalf of the United States, prays that a writ of certiorari issue to review the judgment of the Court of Appeals for the Fifth Circuit.

OPINIONS BELOW

The memorandum decision of the District Court (App., *infra*, p. 15) is reported at 140 F. Supp. 60. The *per curiam* opinion of the Court of Appeals (App., *infra*, p. 14) is reported at 239 F. 2d 384.

JURISDICTION

The judgment of the Court of Appeals (App., *infra*, p. 14) was entered on December 26, 1956. By order of Mr. Justice Black on March 21, 1957, the time for filing a petition for certiorari was extended to April 5, 1957. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254 (1).

QUESTIONS PRESENTED

1. Whether the assignee of an unborn account receivable assigned as collateral security for a contingent obligation not even in potential existence at the time of the assignment is a "mortgagee" (or "pledgee") within the meaning of Section 3672 of the Internal Revenue Code of 1939.

2. Whether an allowance of attorney's fees to an interpleader (the debtor of the taxpayer-assignor) is entitled to priority in the interpleaded fund as against a federal tax lien which had previously attached to the fund.

STATUTE INVOLVED

Internal Revenue Code of 1939:

> SEC. 3670. PROPERTY SUBJECT TO LIEN.
>
> If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, additional amount, or addition to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.
>
> (26 U. S. C., 1952 ed., Sec. 3670.)
>
> SEC. 3671. PERIOD OF LIEN.
>
> Unless another date is specifically fixed by law, the lien shall arise at the time the assessment list was received by the collector and shall continue until the liability for such amount is satisfied or becomes unenforceable by reason of lapse of time.

(26 U. S. C., 1952 ed., Sec. 3671.)

SEC. 3672 [as amended by Sec. 401 of the Revenue Act of 1939, c. 247, 53 Stat. 862, and Sec. 505 of the Revenue Act of 1942, c. 619, 56 Stat. 798]. VALIDITY AGAINST MORTGAGEES, PLEDGEES, PURCHASERS, AND JUDGMENT CREDITORS.

(a) *Invalidity of Lien without Notice.*—Such lien shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the collector—

(1) *Under state or territorial laws.*—In the office in which the filing of such notice is authorized by the law of the State or Territory in which the property subject to the lien is situated, whenever the State or Territory has by law authorized the filing of such notice in an office with the State or Territory; or

* * * * *

(26 U. S. C., 1952 ed., Sec. 3672.)

STATEMENT

This action originated in the District Court of Bexar County, 57th Judicial District of Texas, by the filing of a petition of interpleader by R. F. Ball Construction Company, Inc. (one of the respondents herein). Ball's petition was accompanied by a tender of payment into the registry of court of a fund in the amount of $13,228.55 on behalf of Marcus M. Jacobs Company, Inc. (the taxpayer),[1] a creditor of Ball. The peti-

[1] Prior to October 1, 1951, taxpayer company was organized as a partnership. On that date, the partnership incorporated, and the corporation succeeded to all of the rights and liabilities of the partnership. (R. 23-24.) For convenience, both the partnership and the corporation will be referred to as taxpayer.

tion alleged that the suit was one to quiet title to personal property claimed by (among others) the United States and the Union Pacific Insurance Company (the other respondent), both of whom were named as party defendants. The petition also prayed for the allowance to Ball of attorneys' fees of $500 out of the interpleaded fund. (R. 5–6.) On motion of the United States, the case was removed to the United States District Court for the Western District of Texas. (R. 26.)

1. The pertinent facts, as stipulated (R. 2–9) and as found by the District Court (R. 22–28), may be summarized as follows:

On June 26, 1951, Ball entered into a contract with the Housing Authority of the City of San Antonio, Texas, for the construction of a housing project (TEX 6–10). On July 17, 1951, Ball subcontracted a portion of the work to taxpayer, and required of it a performance bond. (R. 22.)

On July 21, 1951, taxpayer applied to the respondent bonding company for a bond payable to Ball, and, as part of the application, assigned to the bonding company, "as collateral security for the full performance of the covenants and agreements herein contained *and the payment of any other indebtedness or liability of the undersigned to the Company, whether heretofore or hereafter incurred*" (emphasis added), all of their right to any sums (both progress payments and retained percentages) which might become due to them under the subcontract with Ball.[2]

[2] Under the terms of the subcontract, Ball was to retain ten per cent of the value of the completed work at all times until Ball's

The bond was executed on July 23, 1951. (R. 22–23.)

On April 4, 1952, taxpayer applied to the bonding company for a similar performance bond payable to the Darby and Perkins Construction Companies covering a subcontract in Louisville, Kentucky. In the application, taxpayer agreed to indemnify the bonding company against all loss which might be incurred as a result of writing the bond. The bond was executed pursuant to the application, and between December 1953 and March 1954 the bonding company, as surety, was required to make payments totalling $12,971.88 on the Kentucky contract. (R. 24.)

The Government's lien for federal withholding and social security taxes assessed against taxpayer arose in March and May of 1953, when the assessment lists were received by the District Director, and notices of these tax liens totalling $17,010.85 were filed in May, June, and September of 1953. (R. 24–25.)

2. In determining the priorities among the parties[3] to the fund paid into court by Ball, the United States District Court held: (1) that Ball (claiming interpleader's attorneys' fees) was entitled to recover the

work had been accepted by the Housing Authority, at which time the ten per cent retained fund would be paid to taxpayer. (R. 23.)

[3] In addition to the claims presented by Ball, the United States, and the bonding company, two claims were presented by Herweck Company, Inc. (a materialman) and S. H. Kottwitz (an unsecured creditor). The Kottwitz company failed to prosecute its claim, and the bonding company agreed to satisfy the Herweck Company claim in the event it should prevail, thus eliminating (under the court's ruling) the necessity for determining the priority of that claim. (R. 13–14.) Default judgments were also entered against other creditors.

sum of $500; (2) that the bonding company (claiming reimbursement for losses sustained in connection with the Kentucky bond) was entitled to recover the remainder of the fund, less court costs; and (3) that the United States (claiming under the tax liens) was not entitled to any recovery [4] (App., *infra*, p. 30).

In a *per curiam* opinion, the Court of Appeals affirmed the judgment of the District Court for the reasons set forth in the latter's opinion (App., *infra*, p. 14).

REASONS FOR GRANTING THE WRIT

The decision below is in direct conflict with the decisions of this Court holding that the relative priority of a federal tax lien is a federal question; that the classes of lienors ("mortgagee, pledge, purchaser, or judgment creditor") protected by Section 3672 of the Internal Revenue Code of 1939 (*supra*, p. 3) are to be defined in the usual and conventional sense of the terms; that the federal tax lien provided by Section 3670 (*supra*, p. 2) is entitled to priority as against inchoate liens not specifically protected by Section 3672; and that the doctrine of relation back cannot operate to destroy the realities of the situation. *United States* v. *Security Tr. & Sav. Bk.*, 340 U. S. 47; *United States* v. *New Britain*, 347 U. S. 81; *United States* v. *Gilbert Associates*, 345 U. S. 361; *United States* v. *Acri*, 348 U. S. 211; *United States* v. *Liverpool & London Ins. Co.*, 348 U. S. 215; *United States*

[4] It rendered judgment against the Kottwitz and Herweck companies and declared "final" the default judgments previously rendered against various claimants. (R. 30.) See note 3, *supra*.

v. *Scovil*, 348 U. S. 218; *United States* v. *Colotta*, 350 U. S. 808; and *United States* v. *White Bear Brewing Co.*, 350 U. S. 1010.[5] In view of this conflict, and in view of the recurrent character and continuing importance[6] of the problem, a summary reversal of the decision below is, we believe, fully warranted. This, it should be noted, was the disposition in *United States* v. *Colotta, supra,* and *United States* v. *White Bear Brewing Co., supra.*

I. (a) Section 3672 provides that the federal lien "shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the collector * * *." The Court of Appeals, adopting the District Court's reasoning as its own (App., *infra,* p. 14), concluded that, although the bonding company "could be said" to come within the classification of a "pledgee," it "more nearly" came within the classification of a "'mortgagee' under the Texas law" and "[we] therefore hold that the Bonding Company under its assignment as collateral security became a 'mortgagee' within the meaning of [Section] 3672 * * *"[7] (App., *infra,* pp. 21, 23). Thus,

[5] It is also in conflict with *United States* v. *Kings County Iron Works*, 224 F. 2d 232 (C. A. 2d); and *Aetna Casualty & Surety Co.* v. *Horticultural Service*, 1 Misc. 2d 956, reversed on other grounds, 158 N. Y. S. 2d 750.

[6] While the federal liens here involved arose under Sections 3670, 3671, and 3672 of the Internal Revenue Code of 1939, the Internal Revenue Code of 1954 reenacts these provisions without changes material here. See Sections 6321, 6322, and 6323 of the 1954 Code; H. Rep. No. 1337, 83d Cong., 2d Sess., pp. A406–A407; S. Rep. No. 1622, 83d Cong., 2d Sess., pp. 575–576.

[7] With respect to the "purchaser" category in Section 3672, the District Court stated (App., *infra,* p. 20): "* * * I do not rest my

on the basis of the 1951 assignment, the Court of Appeals sustained the bonding company's claim to priority of payment from the interpleaded fund as against the lien of the United States.

The assignment in question was executed in connection with the issuance of a bond pertaining to a building contract to be performed by the taxpayer in Texas. It was executed some nine months prior to issuance of another bond pertaining to a wholly separate building contract to be performed by the taxpayer in Kentucky. Taxpayer defaulted under the Kentucky contract, and about two and a half years after execution of the Texas bond the bonding company was required to make payments under the bond relating to the Kentucky contract. The bonding company then sought repayment on the basis of the taxpayer's 1951 assignment made in connection with the Texas bond. This assignment, after reciting that all sums which might become due taxpayer under the Texas contract were assigned to the bonding company for the full performance of the covenants and agreements therein contained, further recited that such sums were also assigned "as collateral security for * * * the payment of any other indebtedness or liability of the undersigned [taxpayer] to the Company, whether heretofore or hereafter incurred." (R. 22–23.)

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decision on this ground since, in the Scovil case [*supra*] the Supreme Court said: 'A purchaser within the meaning of Section 3672 usually means one who acquires title for a valuable consideration in the manner of vendor and vendee.'" No claim has ever been made that the bonding company falls within the "judgment creditor" category.

This clause, it should be noted, was in no way limited by time, amount, or transaction. At the time of the assignment, not only was the amount assigned (*i. e.*, the account receivable on the Texas contract) neither fixed nor earned, but the contingency on which the assignment depended (*i. e.*, the taxpayer's indebtedness to the bonding company) had not yet arisen. In fact, at that time, it was not known whether there would ever be any indebtedness such as subsequently materialized and, if so, what the amount would be; such indebtedness could hardly even have been contemplated since the bond on the Kentucky contract was not executed until some nine months after the bond on the Texas contract. Several months before the indebtedness materialized in connection with the Kentucky contract, the federal tax liens arose and were duly recorded.

Contrary to the decision below, the assignment does not constitute a "mortgage" (or "pledge") within the meaning of Section 3672. As this Court said (p. 88) in the *New Britain* case, *supra*, which also involved a claim based on the "mortgagee" clause, there is nothing in the language of Section 3672 to show that Congress intended antecedent federal tax liens to rank behind any but the specific categories of interests set out therein.[8] And those specific categories are to be defined in their usual and conventional sense and in a uniform manner in all the states. See *United States* v. *Gilbert Associates*, 345

[8] See also the concurring opinion of Mr. Justice Jackson in *United States* v. *Security Tr. & Sav. Bk.*, 340 U. S. 47, 52, cited in both *Gilbert* (p. 364) and *Scovil* (p. 220).

U. S. 361, 364 ("judgment creditor"); *United States* v. *Scovil*, 348 U. S. 218, 220–221 ("purchaser"). Under that standard, in order to qualify as a "mortgage" (or "pledge") for purposes of Section 3672, surely an assignment to secure an indebtedness must—at the very least—relate to an *existing* indebtedness, not merely an indebtedness that might arise in the future. Here, as already pointed out, the indebtedness secured by the assignment did not come into existence until long after the federal liens were perfected. If such an assignment were to be considered as a "mortgage" (or "pledge") under Section 3672, it is apparent that a taxpayer, by the simple expedient of assigning accounts receivable to another to secure a future indebtedness that may never materialize, could easily thwart the Government in the collection of its taxes.

(b) Adverse liens far more specific and choate than the bonding company's interest here have repeatedly been held by this Court to be subordinate to perfected federal tax liens, even where the adverse liens first arose prior to the federal liens. *Security Tr. & Sav. Bk.* case, *supra* (statutory attachment lien); *Acri* case, *supra* (statutory attachment lien); *Liverpool & London* case, *supra* (statutory garnishment lien); *Scovil* case, *supra* (statutory landlord's distress lien); *Colotta* case, *supra* (statutory mechanic's lien); *White Bear* case, *supra* (statutory mechanic's lien). The courts below sought to distinguish these decisions on the ground that the liens involved there

"arose by virtue of some statutory right, not specifically referred to in Section 3672." But this distinction is based on a misconception of the function of Section 3672. It was not designed to make any exception to the usual rule that a perfected federal tax lien is entitled to priority as against an inchoate lien. Instead, Section 3672 is merely a recordation statute enacted to put lenders, etc., on notice of the federal lien. See *Security Tr. & Sav. Bk.* case, 340 U. S. at 51–53 (concurring opinion). Apart from this notice requirement, there is no basis for assuming that Congress, in enacting Section 3672, intended different priority standards to apply to the designated non-statutory liens than to statutory liens. Thus, the statute would not protect even a true "mortgagee" as to advances made *after* recording of the federal lien.

In this case, the advances for which the bonding company seeks "mortgagee" status were not made until several months after the federal liens had been recorded. Prior to the recording of the federal liens, there was at most a mere possibility that the taxpayer might become indebted to the bonding company. Such a mere possibility is plainly insufficient to constitute a specific and choate lien under this Court's decisions (*supra*). For like reasons, such a mere possibility is insufficient to entitle the bonding company to the status of a "mortgagee" under Section 3672. And, even assuming *arguendo* that the 1951 assignment matured into a "mortgage" (or "pledge") in December 1953 and March 1954 when the bonding company

made its advances, this Court's decisions have also made it clear that the doctrine of relation back will not be permitted to destroy the realities of the situation. See, *e. g.*, the *Security Tr. & Sav. Bk.* case, *supra*, p. 50.

In short, the bonding company is not entitled to "mortgagee" (or "pledgee") status under Section 3672, not only (a) because the assignment on which it relies is not a "mortgage" (or "pledge") within the usual and conventional meaning of the term, but also (b) because the "lien" created by the assignment was unspecific and inchoate at the time the federal tax liens were perfected.

2. A subsidiary question presented in this case is whether the court below properly allowed a fee for the services of the interpleader's attorney to be paid out of the fund impressed with the federal tax lien.[9]

In holding that the fee was allowable, the courts below sought to distinguish the decision of this Court in *United States* v. *Liverpool & London Ins. Co.*, 348 U. S. 215, on the ground that the attorney's fee involved in the *Liverpool* case related to a garnishment suit, not an interpleader action (App., *infra*, pp. 14, 24).

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[9] It is to be noted that the interpleaded fund involved here exceeds the amount claimed by the bonding company, and hence that, even if the bonding company's claim were entitled to priority (as the courts below held), over half of the fund awarded to the interpleader's attorneys was at the expense of the Government.

[10] The case of *United States* v. *Ullman*, 115 F. Supp. 211 (E. D. Pa.), which the court below followed, was decided prior to this Court's decision in the *Liverpool* case; moreover, the *Ullman* case is not "directly in point," as was held below (R. 21), since there the United States had instituted the suit to foreclose its income tax liens. The *Ullman* case is distinguished in *Ford Motor Co.* v. *Hackart Construction Co.*, 143 F. Supp. 216 (N. J.), wherein it

Irrespective of the validity of such a distinction, the fact is that this Court in *Liverpool* characterized the proceeding in that case as an "interpleader action" (p. 216). Moreover, in *Liverpool* as here, the "interpleader action" had been removed from a Texas state court to a United States District Court (*ibid.*). In *Liverpool*, this Court concluded (p. 217) that "* * * certainly fees allowed in that proceeding are not prior to the Government liens, and the authorization of the payment of the attorney's fees prior to the Government liens was error." That holding is plainly controlling here.

CONCLUSION

The questions presented have already been authoritatively settled by this Court in a series of recent decisions. Under those decisions, the decision below is clearly erroneous. It is therefore respectfully submitted that the petition for a writ of certiorari should be granted and the judgment reversed without further briefs or argument.

J. LEE RANKIN,
Solicitor General.

CHARLES K. RICE,
Assistant Attorney General.

A. F. PRESCOTT,
GEORGE F. LYNCH,
Attorneys.

APRIL 1957.

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is pointed out that the decision in the *Ullman* case did not purport to resolve a conflict between a Government lien and an allowance of fees since the question of priorities of interest in the interpleaded fund had not been reached. The decision of this Court in the *Liverpool* case was also followed in *Bruce* v. *United States*, 127 F. Supp. 858 (E. D. Mich.), and *Boston Insurance Co.* v. *Stubbs* (W. D. Wash.), decided March 20, 1956 (1956 C. C. H., par. 9695).

APPENDIX

In The United States Court of Appeals for the Fifth Circuit

No. 16276

UNITED STATES OF AMERICA, APPELLANT

v.

R. F. BALL CONSTRUCTION COMPANY, INC., AND UNITED PACIFIC INSURANCE COMPANY, APPELLEES.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF TEXAS.

(December 26, 1956)

Before CAMERON, JONES and BROWN, Circuit Judges.

Per curiam: The facts of this case are well recited and the controlling principles of law are well stated in the opinion of Judge Rice, *R. F. Ball Construction Company v. Jacobs,* 140 F. Supp. 60. For the reasons there set forth the judgment appealed from is

Affirmed.

JUDGMENT

Extract from the Minutes of December 26, 1956.

[Caption omitted.]

This cause came on to be heard on the transcript of the record from the United States District Court for the Western District of Texas, and was argued by counsel;

On consideration whereof, It is now here ordered and adjudged by this Court that the judgment of the

said District Court appealed from in this cause be, and the same is hereby, affirmed.

United States District Court, Western District of Texas, San Antonio Division

Civil action No. 1997

R. F. BALL CONSTRUCTION COMPANY, INC., PLAINTIFF

vs.

MARCUS M. JACOBS AND HENRY LESKY, d/b/a MARCUS M. JACOBS CO., ET AL., DEFENDANTS

MEMORANDUM OF DECISION

Pursuant to Rule 52 (a) this Memorandum of Decison is filed and contains findings of fact and conclusions of law in this case, the facts of which have all been stipulated by the parties.

On June 26, 1951, R. F. Ball Construction Company (hereinafter called Ball) entered into a contract with the Housing Authority of the City of San Antonio (hereinafter called Housing Authority) for the construction of a housing project. Shortly thereafter Ball subcontracted the painting and decorating involved in such contract to Marcus M. Jacobs Company, a co-partnership consisting of Marcus Jacobs and Henry Leskey [sic] (hereinafter called Jacobs) for the sum of approximately $230,000.00 and required of it a faithful performance bond. On July 21, 1951, Jacobs applied to United Pacific Insurance Company (hereinafter called Bonding Company) for such performance bond, and one of the considerations agreed to in the application for such bond was an unconditional assignment by Jacobs to the Bonding Company of all percentages retained by Ball under the Jacobs subcontract as collateral security for the protection of

the Bonding Company, not only for losses growing out of the Housing job, but for the "payment of any other indebtedness or liability" of Jacobs to the Bonding Company, "whether heretofore or hereafter incurred". A few months thereafter the business of Jacobs was incorporated into Marcus M. Jacobs Company, Inc. (hereinafter called Jacobs, Inc.) and the corporation succeeded to all rights and liabilities of the partnership. No party to this controversy has raised any question about the succession, so this mutation from the partnership to the corporation is immaterial and will not be referred to further. See *Miles* v. *Aetna*, 1 F. Supp. 925; *Illinois Surety Co.* v. *Davis*, 244 U. S. 376, 37 S. Ct. 614, 61 L. Ed. 1202.

Thereafter, on April 4, 1952, Jacobs, Inc. obtained from the Bonding Company a similar bond on another sub-contract in Louisville, Kentucky, in the application for which Jacobs, Inc. agreed "to indemnify and keep indemnified the company against all loss, costs, damages, expenses and attorney's fees whatsoever * * *", and under such bond the Bonding Company exposed itself to a liability of some $35,000.00.

On April 30, 1953, the Housing Authority accepted the work of Ball and subsequently it was agreed between Ball and Jacobs, Inc. that the sum of $13,228.55 representing the retained percentages according to the terms of the sub-contract, was due and owing on this job by Ball to Jacobs, Inc., as of April 30, 1953.

In May, June and September of 1953, and long after the assignment as collateral security of the retained percentages on the Housing Authority job had been made to the Bonding Company, and long after the Bonding Company had executed its obligation under its bond on the Louisville job, the United States Government filed tax liens against Jacobs, Inc. totalling $17,010.85. No stipulation is made by the parties that

this tax claim arose out of Jacobs, Inc.'s failure to pay taxes incurred on either the Housing Authority job or the Louisville job, so that this court must assume that they are ordinary tax liens, not growing out of the particular jobs in question, and the Government here makes no claim on either of the bonds.

After the tax liens had been filed, the potential liability on the Kentucky job incurred by the Bonding Company on April 4, 1952, became an actual liability and the Bonding Company was required to pay, by virtue of its bond in connection with the Kentucky project, the sum of $12,971.88.

Thereafter, because of numerous conflicting claims presented to Ball, Ball was unable to determine with safety to itself to whom the $13,228.55 of retained percentages which it held in its hands should be paid. Therefore, Ball filed this suit, which is an interpleader action, making as parties defendant Jacobs and Jacobs, Inc., the Government, the bonding Company and certain suppliers of materials and services on the Housing Authority job, and asking for an interpleader's fee of $500.00, which has been stipulated to be a reasonable fee if under the law any interpleader's fee is payable. The Government filed its answer claiming the funds by virtue of its tax liens; the Bonding Company filed its answer claiming $12,971.88 of the funds by virtue of its assignment as collateral security and the loss which it sustained on the Kentucky job; the Herweck Company, Inc. filed its claim for $981.83 for materials furnished on the Housing job; S. H. Kottwitz & Company filed its claim for compensation and public liability insurance premiums on said job of $2,431.05. Several other claimants were made parties defendant but failed to answer and make claim, and default judgment was rendered against them. Kottwitz, although filing a claim, has not appeared in any

of the hearings, and has failed to file any briefs herein in support of his claim; and it appearing to the court that under decision such as *U. S.* v. *Yates,* 204 S. W. 2d 399, as well as by virtue of default, Kottwitz is not entitled to recover, judgment will go against him.

The Herweck Company has filed its brief contending that it is entitled to priority, but has likewise stated that the Bonding Company had agreed to satisfy its claim if the Bonding Company prevailed herein, and has asked, therefore, that judgment go in favor of the Bonding Company, and in view of this Herweck likewise goes out of the case, under the court's rulings, since the court is of the opinion that the Bonding Company should prevail herein, and will respect the agreement between Herweck and the Bonding Company.

The principal question for determination by this court is as to which lien is prior—the Government's tax lien which arose by virtue of the filing of the notice of its tax liens in May, June and September of 1953, or the contract lien of the Bonding Company which arose long prior thereto by virtue of the assignment of the retained percentages in question by Jacobs to the Bonding Company, which by contract protected the Bonding Company from the loss which it incurred on the Louisville job, which became a potential loss upon the execution of the Louisville bond on April 4, 1952, prior to the filing of the Government's tax liens, but which was not paid under its bond until after the filing of the Government's tax liens.

The Government cites and contends that the case of *U. S.* v. *Security Trust & Savings Bank,* 340 U. S. 47, 71 S. Ct. 111; *U. S.* v. *Gilbert Associates,* 345 U. S. 361, 73 S. Ct. 701; *U. S.* v. *City of New Britain,* 347 U. S. 81, 74 S. Ct. 367; *U. S.* v. *Acri,* 348 U. S.

211, 75 S. Ct. 239; *U. S.* v. *Liverpool, etc. Ins. Co.*, 348 U. S. 215, 75 S. Ct. 247; and *U. S.* v. *Scovil*, 348 U. S. 218, 75 S. Ct. 244, are in point and are controlling in this case, and says:

> "* * * the principles of *United States* v. *Security Trust & Sav. Bk.*; *United States* v. *New Britain*; *United States* v. *Scovil*; *United States* v. *Acri*; and *United States* v. *Liverpool & London Ins. Co.*, supra, must be applied."

The Bonding Company, on the other hand, contends that none of the liens in the above cited cases were contractual liens and that none of those cases dealt with mortgagees, pledgees, or purchasers within the meaning of Section 3672 of the Internal Revenue Code (now Sec. 6323, Title 26 U. S. C.), and further contends that in those cases the court was construing only the term "judgment creditor" and liens other than mortgages and pledges, and therefore says that such cases are not controlling in this case.

Section 3672 of the Internal Revenue Code provides in effect that filing of a federal tax lien does not affect the rights of any prior "mortgagee, pledgee, purchaser or judgment creditor". Most of the decisions of the Supreme Court cited above and referred to by the Government dealt with inchoate judgment liens and none of those cases dealt with the contract lien of a "mortgagee", "pledgee" or "purchaser". The latter three categories are all based upon a contract right of some sort, whereas the term "judgment creditor" and the other liens dealt with in those cases, such as water rent liens, municipal tax liens and landlord's distress liens, arose by virtue of some statutory right, not specifically referred to in Section 3672.

The Bonding Company contends that since its assignment as collateral security was based upon a contract which was prior in time to the Government's tax

lien, it is either a mortgagee, pledgee or purchaser of the retained funds and it disclaims any contention on its part that it is a judgment creditor, or claims to be anything other than a mortgagee, pledgee or purchaser.

In the case of *National Refining Co.* v. *U. S.*, 106 F. 2d 951, the taxpayer was indebted to National Refining Company, which took an assignment as collateral security from the taxpayer of certain commissions to be earned by him under his contract with the Government "when they should become available to him". Before any money had been earned or paid under this assignment, the Government perfected a tax lien and there claimed that the assignment as collateral security was subordinate. In holding that the assignment to the National Refining Company took priority over the Government's tax claim, the court said:

> "We think it safe to say that one who for a valuable present consideration acquires a property or interest in property, is 'a purchaser' within the meaning of 26 U. S. C. A. Internal Revenue Code, Section 3672."

It cannot be doubted that the execution by the Bonding Company of the bonds in this instance constituted "a valuable present consideration" and it further cannot be doubted that at the time of the assignment as collateral security of the retained percentages by Jacobs to the Bonding Company, the Bonding Company acquired an interest in these retained percentages. However, I do not rest my decision on this ground since in the *Scovil* case the Supreme Court said: "A purchaser within the meaning of Sec. 3672 usually means one who acquires title for a valuable consideration in the manner of vendor and vendee".

In the case of *Knight* v. *Knight*, 71 N. Y. Supp. 2d 357, the Government claimed that its lien for federal

taxes was superior to a prior assignment of future wages as collateral security for payments to the taxpayer's divorced wife. The court there held:

> "The Government attempts to avoid the impact of Section 3672 by contending that respondent is not a pledgee. We think that as the assignment of wages made by defendant Knight was as security for, and a mean of payment of, the defendant's principal obligation to pay plaintiff $20,000.00, the plaintiff comes within the classification of a pledgee."

This case was subsequently affirmed by the Court of Appeals, 80 N. E. 2d 344, and was not appealed by the Government to the Supreme Court of the United States.

The assignment of retained percentages in the case at bar was made by Jacobs as security for and a means of payment of Jacob's obligation to idemnify the Bonding Company against loss, and it could be said therefore, as was held in the *Knight* case, that the Bonding Company "comes within the classification of a pledgee."

In my opinion, however, the Bonding Company in this instance more nearly comes within the classification of a "mortgagee" under the Texas law, which "should be given considerable weight in determining whether or not" the Bonding Company is a mortgagee. See *U. S.* v. *Gargill,* 218 F. 2d 556 at 560. According to 29 Tex. Jur. 786,

> "A mortgage, in the broadest sense of the term, is a pledge of property, either real or personal, or of a chose in action, as security for the performance of an obligation."

According to 29 Tex. Jur. 838,

> "A mortgage which purports to secure future debts is not ineffectual or invalid. On the contrary the lien created will be enforced not only

> in a dispute between the mortgagor and mortgagee but also in a controversy involving the rights of one who claims under the mortgagor."

As was recently stated by the Supreme Court of Iowa in *Evans* v. *Stewart*, 66 N.W. 2d 442 at 449:

> "We feel the requirement that the lienholder be a 'mortgagee' is a requirement of status—that he be in the position of one holding a mortgage."

It is true that the parties to the assignment as collateral security in this instance did not place a label on this transaction as either a mortgage, a pledge or a purchase, but courts do not decide cases on nomenclature; they look to the substance of the transaction; and the substance of the assignment here was to put the Bonding Company in the status of either a mortgagee, pledgee or purchaser, and therefore Section 3672 applies.

In *Northern Nat. Bank* v. *Northern Minn. Nat. Bank*, 70 N. W. 2d 118, the Supreme Court of Minnesota held that an assignment as security of retained percentages under a construction contract to a bank which was prior in time to a Federal tax lien, was superior to the claim of the Government, which is precisely the situation here. The Government did not appeal that case to the Supreme Court of the United States.

The distinction between a contract lien and a statutory lien is made clear by comparing the case of *Evans* v. *Stewart*, supra, with the *Scovil* case, supra. In the *Scovil* case, the Supreme Court held that prior to the time it ripened into a final judgment, an incompleted statutory, landlord's lien was inferior to a federal tax lien, since the holder thereof was neither a "mortgagee", "pledgee", "purchaser" nor "judgment creditor". In the *Evans* case, the court held that a written

contract landlord's lien contained in the lease was superior to a federal tax lien because it was a "mortgage" within 3672. The Government did not appeal the *Evans* case.

The Government argues that if an attachment or other judicial lien is not sufficiently "choate" or complete "to defeat a subsequent tax lien" then a mortgage to secure future indebtedness should likewise be inferior to a subsequent tax lien. Congress has in effect stated in Sec. 3672 that before an attaching, or other similar statutory lien or, could claim priority over the Government, his claim had to ripen into a final judgment. *U. S.* v. *Security Trust, etc.,* supra. *U. S.* v. *Acri,* supra. No such qualification was placed by Congress on the contractual lien of a "mortgagee". It is the Congress which enacts the law with reference to priorities and not the courts, and I therefore hold that the Bonding Company under its assignment as collateral security, became a "mortgagee" within the meaning of 3672 and was, therefore, not affected by the tax liens which were subsequent in time.

While admitting that "the Government does not claim the status of an innocent purchaser for value", the Government does contend that because the Bonding Company did not record its assignment under the provisions of Article 260–1, R. C. S. of Texas, said assignment is therefore inferior to the claim of the Government. In Texas, the recording of an assignment adds nothing to the validity thereof as between the parties. (9 Tex. Jur. 97.)

As I see it, the Government is seeking to read into Section 3672 provisions which Congress has not seen fit to insert therein and the Government would have this court construe such section to read:

> "Such lien shall not be valid as against any mortgagee *whose mortgage is due at a certain*

time and in a certain amount and which mortgage has been duly recorded in accordance with law."

Had Congress seen fit to make such a requirement it could have done so, but I decline to read these words into the statute, and on this point I concur in the opinion of Judge Wyche in the case of *U. S. v. Anders Contracting Company,* 111 F. Supp. 700, where the Government made identically this same contention, was overruled, and did not appeal.

There remains for consideration the question as to whether or not Ball is entitled to any interpleader's fee in this case. The Bonding Company has raised no objection to awarding such fee and in fact has presented cogent arguments as to why such fee should be allowed. The Government, on the other hand, contends that under the case of *U.S. v. Liverpool, etc.,* supra, the interpleader is not entitled to his costs. There can be no question as to the status of Ball in this matter. Ball was an innocent stakeholder confronted with conflicting claims to a fund which was in his hands, and he adopted the proper course of employing attorneys and tendering this money into court. As was said by the Supreme Court in its opinion therein, the *Liverpool* case had to do solely with a garnishee's fee under Rule 677 of the Texas Rules of Civil Procedure and did not purport to deal with an Interpleader action under Texas Rule 43 or Rule 22 of the Federal Rules of Civil Procedure, and it is therefore not controlling. On the other hand, the case of *U. S.* v. *Ullman,* 115 F. Supp. 211, is directly in point, and I adopt the reasoning of the court in that case and hold that Ball is entitled to his interpleader's fee in this case, and the remainder of the interpleaded fund, less costs, should be awarded to the Bonding Company.

The attorneys for the Bonding Company are directed to submit a judgment not inconsistent with this Memorandum.

Done on this 29th day of March A. D. 1956.

(s) BEN H. RICE, JR.
Chief Judge,
United States District Court,
Western District of Texas.

Filed: April 17, 1956.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

(Title Omitted)

FINDINGS OF FACT

1. On June 26, 1951, R. F. Ball Construction Company, Inc. (hereinafter referred to as Ball) entered into a contract with the Housing Authority of the City of San Antonio, Texas, for the construction of Housing Project TEX 6–10.

2. On July 17, 1951, Ball subcontracted the painting and decorating, taping and floating of sheetrock and waterproofing of masonry units on the Housing Project to Marcus M. Jacobs and Henry Lesky, d/b/a Marcus M. Jacobs Co.

3. As a part of the subcontract, Jacobs and Lesky agreed:

> * * * to furnish and pay for all labor, material, tools, equipment, compensation insurance and public liability and property damage insurance (carried in responsible companies and in limits satisfactory to R. F. Ball Construction Company, Inc.), also keep records and make payments on all Federal and/or State Payroll Taxes and/or deductions, together with all other incidentals necessary to complete in a good and workmanlike manner (the subcontracted work) * * *

4. On July 21, 1951, Jacobs and Lesky applied to United Pacific Insurance Company for a faithful performance bond, payable to Ball, in the penal sum of $229,029. The application contained the following clause:

> the undersigned does by these presents assign, transfer and convey to United Pacific Insurance Company, the Company, as of this date, as collateral security for the full performance of the covenants and agreements herein contained and the payment of any other indebtedness or liability of the undersigned to the Company, whether heretofore or hereafter incurred the following:
>
> * * * * *
>
> (d) All right, title and interest of the undersigned in and to and all percentages retained by the Obligee under said contract, and any and all estimates, payments, extras, final payments, and other sums that . . . may be due or may thereafter become due under said contract to or on behalf of the undersigned.

5. On July 23, 1951, Jacobs and Lesky (as principals) and United Pacific (as surety) executed a bond in the amount of $229,029, with Ball as obligee, conditioned upon the faithful performance of the Housing Project subcontract "according to its terms, covenants, and conditions".

6. Under the terms of the subcontract, Ball was to retain 10% of the value of the completed work at all times until Ball's work had been accepted by the Housing Authority, at which time the 10% retained fund would be paid to Jacobs and Lesky.

7. On October 1, 1951, Jacobs and Lesky incorporated their business under the name of Marcus M. Jacobs Company, Inc. and the corporation succeeded to all of the partnership's rights in the Housing Project subcontract. Jacobs' and Lesky's contractual

obligations under the application for the performance bond were binding upon their successors and assigns, which includes the corporation.

8. On April 4, 1952, Marcus M. Jacobs Company, Inc. applied to United Pacific Insurance Company for a bond in the amount of $35,591 payable to the Darby and Perkins Construction Companies covering a subcontract in Louisville, Kentucky. In this application, the corporation agreed to indemnify United Pacific against all loss (including expenses and attorneys' fees) which might be incurred as a result of writing the bond.

9. Pursuant to the application, United Pacific (as surety) and the corporation (as principal) executed a bond and, between December of 1953 and March of 1954, United Pacific, as surety under the bond, was required to make payments totaling $12,971.88.

10. On April 30, 1953, the Housing Authority accepted Ball's work and, pursuant to the subcontract, $13,228.55 (representing the 10% retained by Ball) became due and owing to Marcus Jacobs Company, Inc.

11. The following table sets forth the pertinent information with respect to Marcus Jacobs Company, Inc.'s tax liabilities to the United States:

Kind of tax	Taxable period	Date assessment list received by district director	Date Notice of Tax Liens Filed	Outstanding Balance
W-H	4 Q. '52	3/16/53	6/ 9/53	$6,343.24
FUTA	1952	5/14/53	9/ 5/53	1,012.47
FICA	1 Q. '53	5/15/53	5/18/53	9,655.14
				$17,010.85

12. On July 13, 1953, Herweck Company, Inc. notified United Pacific, the Housing Authority, and Ball that it had a claim against Marcus Jacobs Company, Inc. for $981.83 as a result of paint and other materials furnished in connection with the performance of the subcontract.

13. On September 18, 1953, S. H. Kottwitz & Company notified Ball and United Pacific that it had a claim against Marcus Jacobs Company, Inc. for unpaid insurance premiums in the amount of $2,431.05.

14. On May 24, 1954, Ball commenced this action as an interpleader suit, tendering the $13,228.55 which it owed to Marcus Jacobs Co., Inc., into the registry of the District Court of Bexar County, Texas, asking interpleader's attorneys' fees and costs, to be paid out of the fund. It is agreed between the parties that, if Ball is entitled to receive an interpleader's attorneys' fee as a matter of law, a reasonable sum would be $500.

15. The following parties were named defendants:

Marcus M. Jacobs and Henry Lesky, individually and as partners, d/b/a Marcus M. Jacobs Co.
Marcus M. Jacobs Co., Inc.
United Pacific Insurance Company
Herweck Company, Inc.
Otto Dukes, d/b/a Otto Dukes Machinery Company
Floor Maintenance Bureau Products Company (a corporation)
J. T. Dulaney and R. T. Dulaney, partners, d/b/a Dulaney Service Company
S. H. Kottwitz & Company
The United States of America
R. L. Phinney, District Director of Internal Revenue.

16. The United States of America removed the case to this Court on June 15, 1954, and the $13,228.55

deposited by Ball in the registry of the State Court is now in the registry of this Court.

17. R. L. Phinney, District Director of Internal Revenue, was dismissed as a party.

18. On October 21, 1954, default judgments were entered against the following parties:

Marcus M. Jacobs and Henry Lesky, individually and as partners, d/b/a Marcus M. Jacobs Co.
Marcus Jacobs Co., Inc.
Otto Dukes, d/b/a Otto Dukes Machinery Company
Floor Maintenance Bureau Products Company (a corporation)
J. T. Dulaney and R. T. Dulaney, partners, d/b/a Dulaney Service Company.

19. The remaining parties (Ball, United Pacific, Herweck, Kottwitz, and the United States) submitted the case on a stipulation of facts.

20. The Court must decide what are the relative priorities of the following creditors with respect to the $13,228.55 now on deposit in the registry of this Court representing the retained fund owed by Ball to Marcus Jacobs Co., Inc. as a result of performance of the subcontract on the TEX 6–10 Housing Project:

(a) The United States of America (claiming under tax liens against all property and rights to property belonging to Marcus Jacobs Co., Inc.).

(b) United Pacific Insurance Company (claiming reimbursement for losses sustained as a result of the Louisville bond as assignee of the retained fund earned by Marcus Jacobs Co., Inc. in performing the TEX 6–10 Housing Project subcontract).

(c) Herweck Company, Inc. (an unpaid material man).

(d) S. H. Kottwitz & Company (holding a claim for unpaid insurance premiums).

(e) R. F. Ball Construction Company, Inc. (claiming interpleader's attorneys' fees).

CONCLUSIONS OF LAW

1. Herweck Company, Inc., has not shown that it has any lien on the retained fund in question, as such. Therefore, the claim of Herweck Company, Inc. will be considered an unsecured claim so far as this fund is concerned.

2. S. H. Kottwitz & Company has not shown that it has any lien on the retained fund in question. Therefore, the claim of S. H. Kottwitz & Company will be considered an unsecured claim so far as this fund is concerned.

3. R. F. Ball Construction Company, Inc. under the usual rule, is entitled to interpleader's attorneys' fees out of the fund in question and the parties have stipulated that a reasonable fee in this case is $500. Ball's right to this fee is superior to the tax liens asserted by the United States and to the claim of United Pacific Insurance Company and, therefore, Ball is entitled to receive $500 out of the $13,228.55 now on deposit in the registry of the Court.

4. As between the tax liens asserted by the United States and the assignment claimed by United Pacific Insurance Company, the assignment gave United Pacific an interest in the retained fund which is superior to the Government's tax liens. United Pacific's claim totals $12,971.88 plus expenses and attorneys' fees in connection with the loss sustained under the Louisville bond. United Pacific is therefore entitled to receive the balance of the $13,228.55 on deposit in the registry of the Court after the payment of $500 to Ball and costs.

Done at the request of the government on this 14th day of April, 1956.

(s) BEN H. RICE, JR.
Chief Judge,
United States District Court,
Western District of Texas.

Filed: April 17, 1956.

U. S. GOVERNMENT PRINTING OFFICE: 1957

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In the Supreme Court of the United States

OCTOBER TERM, 1957

No. 97

UNITED STATES OF AMERICA, PETITIONER

v.

R. F. BALL CONSTRUCTION COMPANY, INC., AND UNITED PACIFIC INSURANCE COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The memorandum decision of the District Court (R. 7–14) is reported at 140 F. Supp. 60. The *per curiam* opinion of the Court of Appeals (R. 23) is reported at 239 F. 2d 384.

JURISDICTION

The judgment of the Court of Appeals (R. 24) was entered on December 26, 1956. By order of Mr. Justice Black on March 21, 1957, the time for filing a petition for certiorari was extended to April 5, 1957. (R. 24.) The petition for a writ of certiorari was filed on April 5, 1957, and was granted on May 13,

1957. (R. 25.) The jurisdiction of this Court is invoked under 28 U. S. C. 1254.

QUESTIONS INVOLVED

1. Whether the assignee of an unborn account receivable assigned as collateral security for the payment of an indebtedness not even in potential existence at the time of the assignment is a "mortgagee" (or "pledgee") within the meaning of Section 3672 of the Internal Revenue Code of 1939.

2. Whether an allowance of attorney's fees to an interpleader (the debtor of the taxpayer-assignor) is entitled to priority in the interpleaded fund as against a federal tax lien which had previously attached to the fund.

STATUTES INVOLVED

The pertinent provisions of Sections 3670, 3671, and 3672 (a) of the Internal Revenue Code of 1939, Article 260–1 of 1 Vernon's Civil Statutes of the State of Texas, Annotated, and Article 5490, 16 Vernon's Civil Statutes of the State of Texas, Annotated, are set forth in the Appendix, *infra*, pp. 27–29.

STATEMENT

This action originated in the District Court of Bexar County, 57th Judicial District of Texas, by the filing of a petition of interpleader by R. F. Ball Construction Company, Inc. (one of the respondents herein). Ball's petition was accompanied by a tender of payment into the registry of court of a fund in the amount of $13,228.55 on behalf of Marcus M. Jacobs

Company, Inc. (the taxpayer),[1] a creditor of Ball. The petition alleged that the suit was one to quiet title to personal property claimed by (among others) the United States and the United Pacific Insurance Company (the other respondent), both of whom were named as party defendants. The petition also prayed for the allowance to Ball of attorneys' fees of $500 out of the interpleaded fund. (R. 4, 17.) On motion of the United States, the case was removed to the United States District Court for the Western District of Texas. (R. 18.)

The pertinent facts, as stipulated (R. 1–6) and as found by the District Court (R. 15–19), may be summarized as follows:

On June 26, 1951, Ball entered into a contract with the Housing Authority of the City of San Antonio, Texas, for the construction of a housing project (TEX 6–10). On July 17, 1951, Ball subcontracted a portion of the work to taxpayer and required of it a performance bond.[2] (R. 15.)

On July 21, 1951, taxpayer applied to the respondent bonding company for a bond payable to Ball, and, as part of the application, assigned to the bonding company, "*as collateral security for* the full performance of the covenants and agreements herein contained and *the payment of any other indebtedness or liability*

[1] Prior to October 1, 1951, taxpayer company was organized as a partnership. On that date, the partnership incorporated, and the corporation succeeded to all of the rights and liabilities of the partnership. (R. 16.) For convenience, both the partnership and the corporation will be referred to as taxpayer.

[2] This bond also covered another housing project (TEX 6–7). (R. 2.)

of the undersigned to the Company, whether heretofore or hereafter incurred" (emphasis added), all of their right to any sums which might become due to them under the subcontract with Ball.[3] The bond was executed on July 23, 1951. (R. 15–16).

On April 4, 1952, taxpayer applied to the bonding company for a similar performance bond payable to the Darby and Perkins Construction Companies covering a subcontract in Louisville, Kentucky. In the application, taxpayer agreed to indemnify the bonding company against all loss which might be incurred as a result of writing the bond. The bond was executed pursuant to the application, and between December 1953 and March 1954 the bonding company, as surety, was required to make payments totaling $12,971.88 on the Kentucky contract. (R. 16.)

The Government's liens for federal withholding and social security taxes assessed against taxpayer arose in March and May of 1953, when the assessment lists were received by the District Director, and notices of these tax liens totaling $17,010.85 were filed in May, June, and September of 1953. (R. 16–17.)

In determining the priorities among the parties[4] to the fund paid into court by Ball, the United States

[3] Under the terms of the subcontract, Ball was to retain ten per cent of the value of the completed work at all times until Ball's work had been accepted by the Housing Authority, at which time the ten per cent retained fund would be paid to taxpayer. (R. 16.)

[4] In addition to the claims presented by Ball, the United States, and the bonding company, two claims were presented by Herweck Company, Inc. (a materialman) and S. H. Kottwitz (an unsecured creditor). The Kottwitz company failed to prosecute its claim, and the bonding company agreed to satisfy

District Court held: (1) that Ball (claiming interpleader's attorneys' fees) was entitled to recover the sum of $500; (2) that the bonding company (claiming reimbursement for losses sustained in connection with the Kentucky bond) was entitled to recover the remainder of the fund, less court costs; and (3) that the United States (claiming under the tax liens) was not entitled to any recovery.[5] (R. 19.)

In a *per curiam* opinion, the Court of Appeals affirmed the judgment of the District Court for the reasons set forth in the latter's opinion. (R. 23.)

SUMMARY OF ARGUMENT

I

A. The court below erred in holding that taxpayer's assignment of unearned, though potential, income under the Texas contract was a mortgage within the scope of Section 3672 of the Internal Revenue Code of 1939, and that the assignment secured, as of the date of its execution, the indebtedness which subsequently arose under an entirely different and unrelated contract (the Kentucky contract). The term "mortgagee" as used in Section 3672 is to be understood in its conventional sense. In that sense, a mortgage must not only be security for a debt to which it is collateral,

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the Herweck Company claim in the event it should prevail, thus eliminating (under the court's ruling) the necessity for determining the priority of that claim. Default judgments were also entered against other creditors. (R. 8–9.)

[5] It also rendered judgment against the Kottwitz and Herweck companies (see note 4, *supra*) and declared "final" the default judgments previously rendered against various claimants. (R. 20.)

but there must also be in existence specific property to which the mortgage lien can attach. Here, at the time taxpayer assigned the unearned income under the Texas contract, he had nothing to assign; neither was he indebted to the respondent surety company at that time. Hence, at the time of its execution, the assignment was not a mortgage.

Even if the assignment be deemed as intended to effect a mortgage of after-acquired property, it was of no legal effect as such until an indebtedness arose several years later in consequence of the default under the Kentucky contract. Until that time, the *amount* of the lien was not known and could not have been determined from the vague reference in the assignment to "any other indebtedness." Until that indebtedness had been determined, the bonding company had at most only an inchoate and unperfected lien. Prior to that time, however, all the federal tax liens had arisen and were recorded. In such circumstances, the priority of the federal liens is clear from several recent decisions of this Court holding, *inter alia*, that an adverse lien must be specific and perfected at the time the tax lien arises in order to prime a federal tax lien and that the doctrine of relation-back cannot operate to destroy the realities of the situation.

B. Nor is the purported assignment a pledge in its conventional sense. There was no transfer of possession, either actual or constructive, of property or collateral sought to be pledged as security.

II

The courts below also erred in allowing an attorney's fee to be paid to the interpleader's attorney out

of the fund in question. Since the fund was impressed with a prior and perfected lien of the United States, attorney's fees arising thereafter are subordinate to the Government's liens. In this aspect, the case is controlled by *United States* v. *Liverpool & London Ins. Co.*, 348 U. S. 215.

ARGUMENT

I

A FEDERAL TAX LIEN IS SUPERIOR TO AN INCHOATE LIEN BASED UPON THE ASSIGNMENT OF AN UNBORN ACCOUNT RECEIVABLE AS COLLATERAL SECURITY FOR A CONTINGENT OBLIGATION WHICH DID NOT RIPEN INTO INDEBTEDNESS UNTIL AFTER THE RECORDING OF THE FEDERAL LIEN

The principal question to be determined in this case involves the relative priority to be accorded a surety's claim based upon the assignment of an unborn account receivable, as against certain federal tax liens which arose under the provisions of Sections 3670 and 3671 of the Internal Revenue Code of 1939 (Appendix, *infra*, p. 27).

Section 3670 provides that, if any person liable to pay any tax neglects or refuses to pay the same after demand, the amount "shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person." Section 3671 provides that, unless another date is specifically fixed by law, "the lien shall arise at the time the assessment list was received by the collector [District Director] and shall continue until the liability for such amount is satisfied or becomes unenforceable by reason of lapse of time."

Accordingly, the tax liens here involved arose on March 16, May 14, and May 15, 1953, the dates on which the District Director received the assessment lists assessing the taxes involved in the total amount of $17,010.85. (R. 16–17.) When, on April 30, 1953, the Housing Authority accepted the work under the Texas contract, taxpayer became entitled to receive the sum of $13,228.55, representing the retained percentages under its subcontract with the Ball Construction Company. Consequently, as of May 15, 1953, when the last of the three tax liens arose, the Government had perfected tax liens on the $13,228.55 debt owed by Ball to taxpayer. *United States* v. *New Britain*, 347 U. S. 81. Notices of these federal liens, moreover, were filed in May, June, and September, 1953.

The assignment, under which the bonding company claims, was made on July 21, 1951, in connection with the issuance of a bond pertaining to a building subcontract to be performed by the taxpayer in Texas. It was executed some nine months prior to issuance of another bond pertaining to an entirely different contract to be performed by taxpayer in Kentucky. As stated above, that Texas contract was completed on April 30, 1953, and taxpayer incurred no liability thereunder for which the bonding company was liable. But taxpayer defaulted under the Kentucky contract, and between December 1953 and March 1954—about two and a half years after execution of the Texas bond on July 23, 1951—the bonding company was required to make payments under the bond relating to the Kentucky contract in the amount of $12,971.88.

(R. 15–16). The bonding company then sought repayment on the basis of the taxpayer's assignment made in connection with the Texas bond.

That assignment, after reciting that all sums which might become due taxpayer under the Texas contract were assigned to the bonding company for the full performance of the covenants and agreements therein contained, further recited that such sums were also assigned "as collateral security for * * * the payment of any other indebtedness or liability of the undersigned [taxpayer] to the Company, whether heretofore or hereafter incurred."[6] (R. 15.) The phrase "other indebtedness," as construed by the courts below,[7] is in no way limited by time, amount, or transaction. At the time of the assignment, not only was the amount assigned (*i. e.*, the account receivable on the Texas contract) neither fixed nor earned, but the contingency on which the assignment depended (*i. e.*, the taxpayer's indebtedness to the bonding company) had not yet arisen. In fact, at that time, it was not known whether there would ever be any indebtedness such as subsequently materialized and, if so, what the amount would be; such indebtedness could hardly have even been contemplated since,

[6] The record contains no evidence of any past indebtedness.

[7] The courts below concluded that the phrase encompassed the indebtedness which subsequently arose between the taxpayer and the bonding company in connection with the entirely independent *Kentucky* contract. The Government argued that such a construction is erroneous, particularly when considered in light of the fact that a separate bond indemnifying the bonding company was executed in connection with the *Kentucky* contract. (R. 5, 16.) See *Belton* v. *Bank*, 186 N. C. 614; *Wright* v. *Voorhees*, 131 Ia. 408.

as already pointed out, the bond on the Kentucky contract was not executed until some nine months after the bond on the Texas contract. "Nor can the doctrine of relation back * * * operate to destroy the realities of the situation." *United States* v. *Security Tr. & Sav. Bk.*, 340 U. S. 47, 50.

However, on the basis of Section 3672 (a) of the 1939 Code (Appendix, *infra*, p. 27), the Court of Appeals sustained the bonding company's claim to priority of payment from the interpleaded fund as against the tax liens of the United States. The Court of Appeals, adopting the District Court's reasoning as its own (R. 23), concluded that, although the bonding company "could be said" to come within the classification of a "pledgee," it "more nearly" came within the classification of a "'mortgagee' under the Texas law" and "[we] therefore hold that the Bonding Company under its assignment as collateral security became a 'mortgagee' within the meaning of [Section] 3672 * * *" (R. 11–12, 13).* This, we submit, was error.

Apart from Section 3672, it is clear that the bonding company's claim to priority of payment must fail; for under no circumstances can it be said that the bonding company's interest "attached to the property

* With respect to the "purchaser" category in Section 3672, the District Court stated (R. 11): "* * * I do not rest my decision on this ground since, in the *Scovil* case [348 U. S. 218] the Supreme Court said: 'A purchaser within the meaning of Sec. 3672 usually means one who acquires title for a valuable consideration in the manner of vendor and vendee.'" No claim has ever been made that the bonding company falls within the "judgment creditor" category.

in question and became choate" before the federal tax liens. *United States* v. *New Britain, supra,* pp. 85–86. Section 3672 (a) provides that such federal tax liens "shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the collector." As this Court stated in the *New Britain* case, *supra,* p. 88, which also involved a claim based on the "mortgagee" clause, there is nothing in the language of Section 3672 to show that Congress intended antecedent federal tax liens to rank behind any but the specific categories of interests set out therein. These specific categories, moreover, are to be defined in their usual and conventional sense and in a uniform manner in all the states. See *United States* v. *Gilbert Associates,* 345 U. S. 361, 364; *United States* v. *Scovil,* 348 U. S. 218, 220–221.[9] As shown below, the taxpayer's assignment to the bonding company does not constitute a "mortgage" (or "pledge") within the meaning of Section 3672 (a),[10] and accordingly the federal tax liens are entitled to priority.

A. THE ASSIGNMENT IS NOT A MORTGAGE WITHIN THE MEANING OF SECTION 3672 (a)

As stated in 4 Pomeroy, *Equity Jurisprudence* (5th ed.), pp. 565–566, a concise definition of mortgage is virtually impossible because of its double character—namely, "that it is both a lien in equity and a con-

[9] See also the concurring opinion of Mr. Justice Jackson in *United States* v. *Security Tr. & Sav. Bk.,* 340 U. S. 47, 52–53, cited in both *Gilbert* (p. 364) and *Scovil* (p. 220).

[10] See note 8, *supra.*

veyance at law." Various definitions, however, have been advanced by the commentators and the courts.

Thus, 1 *Jones on Mortgages* (8th ed.), Section 17, quotes Kent's definition as follows: "A mortgage is the conveyance of an estate by way of pledge for the security of a debt, and to become void on payment of it." In 1 Jones, *Chattel Mortgages and Conditional Sales*, p. 6, the author states that, under either the conveyance of title or creation of lien theory, "a chattel mortgage may be defined as a transfer of some present legal or equitable right in personal property, as security for the payment of money, or for the performance of some other act." 1 *Glenn on Mortgages*, p. 3, gives a modern definition of mortgage as "any form of instrument whereby a lien is created upon real estate or whereby title to real estate is reserved or conveyed as security for the payment of a debt or fulfillment of other obligation."

In *Conrad* v. *Atlantic Insurance Co.*, 1 Pet. 386, 441, it was stated that a mortgage is not only a lien for a debt, but also "it is a transfer of the property itself, as security for the debt." In a later case, *Terrell* v. *Allison*, 21 Wall. 289, this Court pointed out (p. 293) that a mortgage in most states is not regarded as a conveyance, but is treated as a mere lien or encumbrance upon the property as security for the payment of a debt or the performance of some other pecuniary obligation. See to the same effect *Platt* v. *Union Pacific R. R. Co.*, 99 U. S. 48;

cf. *New York* v. *Maclay*, 288 U. S. 290, 294.[11] Thus, in *United States* v. *New Britain*, 347 U. S. 81, 84, this Court described a mortgage as a "specific lien."

In substance, however, a mortgage is but a security for a debt, or an obligation, to which it is collateral. *Brobst* v. *Brock*, 10 Wall. 519, 529. While no precise form of words is necessary to constitute a mortgage, it must evidence a present purpose of the mortgagor to pledge his property for the payment of a sum of money, or for the performance of some other act, or it cannot be construed as a mortgage. *N. O. Nat. Banking Ass'n* v. *Adams*, 109 U. S. 211, 214. Without any debt or obligation secured by it, the mortgage instrument can have no present legal effect as a mortgage; the instrument can only take effect as a mortgage from the time some debt or liability shall have been created. *Ladue* v. *The Detroit & Milwaukee Railroad Co.*, 13 Mich. 380, 397. Moreover, the lien must attach to "specific property" of the debtor. *Illinois* v. *Campbell*, 329 U. S. 362, 373; and see *Conrad* v. *Atlantic Insurance Co.*, 1 Pet. 386, 441. Thus, as Glenn, *supra*, p. 18, points out, a mortgage implies more than a debt or other obligation: "there must also be specific security" and this means "not a promise to furnish collateral, but collateral actually transferred." The author then refers to a promise

[11] This is the rule in Texas. *Humble Oil & Refining Co.* v. *Atwood*, 150 Tex. 617, 624, certiorari denied, 345 U. S. 970. Until foreclosure, title and possession remain in the mortgagor. *In re Thomas*, 36 F. 2d 221 (C. A. 5th); *Willis* v. *Moore*, 59 Tex. 628, 635. An assignment, on the other hand, disposes of the entire property. *Preston* v. *Carter Bros. & Co.*, 80 Tex. 388, 390.

to furnish collateral or security "as creating an equitable mortgage or lien" and adds that use of the adjective "equitable" shows, "that the things which lie in promise are not the same as an *actual mortgage*. The latter requires a transfer or other transaction which results in the lender acquiring *an actual interest*, cognizable at law, *in a definite object of property*." (Emphasis added.)

The assignment transaction with which this case is concerned does not meet this test of an "actual" mortgage. At the time of the assignment, the Texas subcontract was wholly executory and no sums had been earned or were due the taxpayer-assignor thereunder. The taxpayer, therefore, did not own any existing property or have an existing chose in action to offer or transfer to the bonding company as "specific security" for the performance of the contractual obligations or for payment of "other indebtedness." The property here in question—taxpayer's right to the sum of $13,228.53, representing the retained percentages under the contract with the Ball Construction Company—did not come into existence until April 30, 1953, when the work under the Texas subcontract had been performed and accepted.[12]

Furthermore, even on the latter date, there was no debt or obligation in existence which could be the subject of a mortgage. As stated in *Frentel* v.

[12] Of course, where no rule of law is infringed and the rights of third persons are not prejudiced, courts of equity will, in proper cases, give effect to a mortgage of after-acquired property. See, *e. g.*, *Penrock* v. *Coe*, 23 How. 117, 128. Such mortgages, however, constitute only an executory agreement that the future-acquired property shall serve as security from and after the time it comes into existence; otherwise stated, the lien of a mortgage on after-acquired property of the mortgagor

Schmitz, 299 Ill. 320, 323: "A mortgage is security for a debt and without a debt it has no effect as a lien. * * * [T]he lien begins only when money is advanced or the contemplated debt comes into existence in the course of dealing between the parties."[13] Since no debt arose between the taxpayer and the surety until the bonding company was required to

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attaches only when the property comes into existence. See, *e. g.*, *Beall* v. *White*, 94 U. S. 382.

As just pointed out in the text, the after-acquired property here did not come into existence until April 30, 1953. At that very moment, the taxpayer's right to the $13,238.53 became subject to the federal tax lien which had arisen on March 16, 1953. This lien immediately attached to the after-acquired property. *Glass City Bank* v. *United States*, 326 U. S. 265. And, even if there had been an adverse lien which had attached simultaneously, the federal lien would take first. *United States* v. *Graham*, 96 F. Supp. 318, 321 (S. D. Calif.), affirmed *per curiam*, *sub nom.* *State of California* v. *United States*, 195 F. 2d 530 (C. A. 9th), certiorari denied, 344 U. S. 831.

Moreover, even a mortgage of after-acquired property requires a debt (or other obligation) as the subject of the mortgage. Here the debt did not arise until the period between December 1953 and March 1954—long after the federal tax liens had been recorded.

[13] See also 1 *Jones on Mortgages* (8th ed.), pp. 601–602; 3 *Glenn on Mortgages*, Sections 396, 400; *United States* v. *Phillips*, 198 F. 2d 634 (C. A. 5th); *In re New York, S. & W. R. Co.*, 109 F. 2d 988 (C. A. 3d), certiorari denied, 310 U. S. 633; *Ky. Lbr. & Mill W. Co.* v. *Ky. Title S. B. & T. Co.*, 184 Ky. 241; *Ginsberg* v. *Capitol City Wrecking Co.*, 300 Mich. 712, 718; *Kommel* v. *Herb-Giner Const. Co.*, 256 N. Y. 333.

Although, as applied to indemnity mortgages, there is authority (see 1 *Jones on Mortgages*, *supra*, Section 467, and cases cited) holding that the lien of such a mortgage takes effect from the time of its execution and delivery (particularly where an obligation to incur future liabilities exists), such authority has no standing in cases involving federal tax liens for, as this Court has said, the doctrine of relation-back has no application in such cases. *United States* v. *Security Tr. & Sav. Bk.*, 340 U. S. 47, 50.

make payments under the Kentucky bond—between December 1953 and March 1954—no lien or mortgage would have arisen until that time. Prior to that time, however, notices of all the federal liens had been filed. In such circumstances, the federal liens prime any rights of the bonding company to the fund in question.

In fact, prior to the time the indebtedness arose between taxpayer and the bonding company, the assignment agreement was not even a "*caveat* of a more perfect lien to come." Cf. *United States* v. *Security Tr. & Sav. Bk., supra,* p. 50; *United States* v. *Scovil,* 348 U. S. 218, 220; *United States* v. *Waddill Co.,* 323 U. S. 353, 357. *New York* v. *Maclay,* 288 U. S. 290, 294. As in the case of an "open-end mortgage" covering future advances,[14] an indebtedness might never have been incurred under the assignment. The possibility of such an indebtedness was problematical and remote, for it depended on whether the taxpayer defaulted in performance of the Kentucky contract. Until such default took place and the amount of the indebtedness was established, there could be no perfected lien under federal law. This Court has declared it to be the rule that a lien must be definite, not merely ascertainable in the future by taking further steps to perfect it, and that in this sense a lien might be said to be perfected when there is established the identity of the lienor, the property subject to the lien, and the amount of the lien. *Illinois* v. *Campbell,* 329 U. S. 362, 375; *United States* v. *New Britain,*

[14] See note 16, *infra.*

supra, p. 84. Assuming that the identity of the lienor and the property subject to the lien were established, it is clear that the *amount* of the lien was not established, and could not have been established, until the default—long after the intervening federal tax liens arose and were recorded.

In addition, with respect to a mortgage for future advances, it is the general rule that, although the amount of the intended advances need not be stated, nevertheless the contemplated debt must be sufficiently described so that it may be recognized and distinguished from other debts. Otherwise, the mortgage will be void on the ground of uncertainty in the description of the demand or liability intended to be included.[15] As stated in 1 *Jones on Mortgages*, *supra*, p. 595:

> There must be some limit to the amount which the mortgage is to secure, either by express limitation or by stating generally the object of the security.
>
> *If the limit be not defined in any way, it can* be good only for the advances made at the time, and such others as may afterward be made before any other incumbrances are made upon

[15] See 1 Jones, *Chattel Mortgages and Conditional Sales*, *supra*, Sections 86, 95; 1 *Jones on Mortgages*, Sections 425-428, 447, *et. seq.*; *Lawrence* v. *Tucker*, 23 How. 14; *Shirras* v. *Caig*, 7 Cranch 34; *United States* v. *Hooe*, 3 Cranch 73; *Douglass* v. *Reynolds*, 7 Pet. 113; *Townsend* v. *Todd et al.*, 91 U. S. 452; *National Finance Co.* v. *Fregia*, 78 S. W. 2d 1081, 1082 (Tex. Civ. App.); *Allen* v. *Lathrop & Co.*, 46 Ga. 133; *Beach* v. *Osborne*, 74 Conn. 405; *Bowen* v. *Ratcliff*, 140 Ind. 393, 396-397; *Moran* v. *Gardemeyer*, 82 Cal. 96.

> the property mortgaged. A mortgage which merely declares that it is to secure such advances as shall thereafter be made by the mortgagee to the mortgagor, or such indebtedness as shall thereafter arise between them, should, it would seem, be held invalid either as against the policy of the law or as constituting evidence of fraud.

In the instant case, the "other indebtedness," as the assignment is construed by the courts below, is not described or limited in any way, either as to amount, purpose, or time. It therefore can not even be regarded as a valid mortgage for future advances. See *Wright* v. *Voorhees*, 131 Ia. 408, 410–411. A contrary holding would only invite the use of such assignments for the perpetration of fraud upon creditors, including the United States. *New* v. *Sailors*, 114 Ind. 407, 410; *Pettibone* v. *Griswold*, 4 *Conn.* 158, 162.

Moreover, Section 3672 (a) affords no protection, we believe, to mortgages for future advances, but rather only mortgages securing existing debts.[16] Until an advance is actually made, there can be no fixed and specific or perfected lien under federal law as dis-

[16] This is the position taken by the Internal Revenue Service in a recent ruling. Rev. Rul. 56–41, 1956–1 Cum. Bull. 562. There the Service was requested to rule whether an advance of money by a mortgagee under an "open-end mortgage" subsequent to the original loan had priority over an intervening recorded federal tax lien. An "open-end mortgage" was described as a mortgage with a future advance clause providing for increasing an existing mortgage debt—the loan or advance subsequent to the original loan being secured by the same mortgage.

tinguished from a mere contingent lien or "caveat of a more perfect lien to come," and consequently an intervening recorded federal tax lien should have priority over advances made subsequent to the date of such recording. The correctness of this position is reflected in several decisions of this Court where actual adverse liens—far more specific than the bonding company's interest here—have been held subordinate to perfected federal tax liens, even where the adverse liens arose prior to the federal liens.

Thus, in *United States* v. *Security Tr. & Sav. Bk.*, 340 U. S. 47, federal tax liens recorded prior to the time a statutory attachment lien was perfected by judgment were held entitled to priority. In its opinion, this Court pointed out (p. 50) that "numerous contingencies" might arise which would prevent the attachment lien from ever becoming perfected by judgment, and consequently that the attachment lien was inchoate. The principles of the *Security Tr. & Sav. Bk.* case, *supra,* were also applied by this Court in *United States* v. *Acri,* 348 U. S. 211, which also involved a statutory attachment lien; in *United States* v. *Liverpool & London Ins. Co.,* 348 U. S. 215, involving a statutory garnishment lien; in *United States* v. *Scovil,* 348 U. S. 218, involving a statutory landlord's distress lien; and in *United States* v. *Colotta,* 350 U. S. 808, and *United States* v. *White Bear Brewing Co.,* 350 U. S. 1010, both of which involved statutory mechanics liens.

The court below sought to distinguish the cited cases, as well as *United States* v. *Gilbert Associates,* 345 U. S. 361, and *United States* v. *New Britain,* 347

U. S. 81, both of which dealt with adverse municipal tax liens, on the ground that (R. 10) the liens involved in those cases "arose by virtue of some statutory right, not specifically referred to in Section 3672," whereas the liens of a "mortgagee,"[17] "pledgee," or "purchaser" "are all based upon a contract right of some sort." The attempted distinction, however, is based upon a misconception of the purpose and function of Section 3672. That section was originally enacted in 1913 (37 Stat. 1016) as an amendment of Revised Statutes, Section 3186, and was occasioned by the decision of this Court in *United States* v. *Snyder*, 149 U. S. 210. See S. Rep. No. 1315, 62d Cong., 3d Sess. The *Snyder* case held that the tax lien created by Section 3186 was valid even as against a bona fide purchaser or incumbrancer in good faith, though he had no notice of the tax delinquency of the person through whom he acquired his title or lien. The purpose of the 1913 amendment was to protect a mortgagee, purchaser, or judgment creditor[17] against this comprehensive secret lien of the United States, by providing that it should not be valid as against such persons until recorded. Section 3672, therefore, is merely a recordation statute enacted to give the particular classes of lienors specified therein notice of the existence of a federal tax lien. See *United States* v. *Security Tr. & Sav. Bk.*, *supra*, pp. 51–53 (concurring opinion). It was not designed or intended to make any exception to the rule that a perfected

[17] The term "pledgee" was added to Section 3672 of the Internal Revenue Code of 1939 by Section 401 of the Revenue Act of 1939, c. 247, 53 Stat. 862.

tax lien is entitled to priority as against an inchoate lien, and there certainly is no basis for assuming, as did the court below, that in enacting Section 3672 Congress intended different priority standards to apply to the designated nonstatutory liens than to statutory liens.

In this case, as already shown, the advances for which the bonding company seeks "mortgagee" status were not made until several months after the federal liens had been recorded. Prior to the recording of the federal liens, there was at most a mere possibility that the taxpayer might become indebted to the bonding company. Such a mere possibility is plainly insufficient to constitute a specific lien under this Court's decisions (*supra*, p. 19). For like reasons, such a mere possibility is insufficient to entitle the bonding company to the status of a "mortgagee" under Section 3672. "Nor can the doctrine of relation back * * * operate to destroy the realities of the situation." *United States* v. *Security Tr. & Sav. Bk.*, *supra*, p. 50. The bonding company therefore is hardly in the position of a bona fide purchaser or incumbrancer who in good faith makes advances without notice of a secret lien of the United States. In the situation involved here, the purpose and function of Section 3672 (see *supra*, p. 20) have no application.

B. THE ASSIGNMENT IS NOT A PLEDGE WITHIN THE MEANING OF SECTION 3672 (a)

As previously pointed out, the courts below were of the view that, by virtue of the assignment, the bonding company "could be said" to come within the classification of a "pledgee" under Section 3672 (a),

although the decision was specifically placed on the ground that the bonding company was a "mortgagee."

Whether a particular instrument be a mortgage or pledge, the purpose of the instrument is the same—to secure the payment of money, or the performance of some act by the maker of the instrument. There is, nevertheless, a well-recognized distinction between the two. Not only must a pledge secure a debt or other obligation, but furthermore it must be accompanied by a transfer of possession of the property or collateral pledged as security. *Casey* v. *Cavaroc*, 96 U. S. 467;[18] *Third Nat. Bank* v. *Buffalo German Ins. Co.*, 193 U. S. 581, 588; *Security Warehousing Co.* v. *Hand*, 206 U. S. 415, 421; *Dale* v. *Pattison*, 234 U. S. 399; *Bostian* v. *Park National Bank*, 226 F. 2d 753, 756 (C. A. 8th); *First National Bank* v. *McCamey*, 130 Tex. 148, 152; *Central Nat. Bank* v. *Latham & Co.*, 22 S. W. 2d 765 (Tex. Civ. App.); 1 Jones, *Chattel Mortgages and Conditional Sales*, *supra*, pp. 10–12; and 10 Am. Jur., *Chattel Mortgages*, Section 10, pp. 723–724. In the *Cavaroc* case, *supra*, where this Court distinguished a mortgage and a pledge, it said (p. 477): "Indeed, possession may be considered as of the very essence of a pledge * * *." And later in the *Security Warehousing Co.* case, *supra*, it stated (p. 421): "The general law of pledge requires possession, and it cannot exist without it." Of course, where the property or collateral is from its character or situation incapable of actual delivery, there may be a constructive or sym-

[18] See also *Casey* v. *Schuchardt*, 96 U. S. 494, and *Casey* v. *Schneider*, 96 U. S. 496.

bolic transfer of the property and right to possession *Dale* v. *Pattison, supra,* pp. 408–409; *Casey* v. *Cavaroc, supra,* p. 477.

At the time the assignment in the instant case was executed, taxpayer was not entitled to receive the retained percentages and hence had nothing which could be the subject of a present assignment or pledge. And, in order to have an "equitable" assignment there would have to be such an appropriation of the retained percentages that the holder of the fund (Ball) would be authorized to pay the amount directly to the creditor; more succinctly stated, "an equitable assignment can be effected only by surrender of control over the funds or property assigned." *Central Nat. Bank* v. *Latham & Co., supra,* p. 767. Here, there was no order of appropriation of the funds or any evidence of surrender of control over them. Viewed as a contract of pledge, the agreement remained wholly executory. *Third Nat. Bank* v. *Buffalo German Ins. Co., supra.*

In fact, insofar as concerns the bonding company, Ball was entirely free to pay over the retained percentages to the taxpayer when the Texas contract was completed and accepted on April 30, 1953. As stipulated (R. 2–3) and found by the trial court (R. 8), those retained percentages were "due and owing" to the taxpayer on that date. Except for the fact that shortly thereafter Ball was presented with notices of claims of creditors of the taxpayer (R. 3–4, 8–9), those funds could have been paid to the taxpayer in the ordinary course of events long prior to the time

any indebtedness arose in connection with the Kentucky contract.

In addition, what has been said above with reference to a mortgage (*supra*, pp. 11–21) is equally applicable to show that the bonding company was not a "pledgee" as that term is used in Section 3672 (a).

II

THE COURT BELOW ERRED IN ALLOWING A FEE FOR THE INTERPLEADER'S ATTORNEY OUT OF THE FUND IMPRESSED WITH THE FEDERAL TAX LIENS

The fund in question was paid into court by the Ball Construction Company, which named as parties the taxpayer, the United States, the bonding company, and certain suppliers of materials and services. In its complaint, Ball asked for the allowance of an interpleader's attorney's fee payable from the fund. It was stipulated among the parties that, if such a fee were allowable, $500 was a reasonable amount. (R. 4, 8.)

The courts below held that the fee was allowable and that Ball's right to the fee was superior to the tax liens asserted by the United States and to the claim of the bonding company. (R. 19.)[12] In so holding, the courts sought to distinguish the decision of this Court in *United States* v. *Liverpool & London Ins. Co.*, 348 U. S. 215, on the ground that (R.

[12] It is to be noted that the interpleaded fund involved here exceeds the amount claimed by the bonding company, and hence that, even if the bonding company's claim were entitled to priority (as the courts below held), over half of the fund awarded to the interpleader's attorneys was at the expense of the Government.

14) it "had to do solely with a garnishee's fee under Rule 677 of the Texas Rules of Civil Procedure and did not purport to deal with an interpleader action under Texas Rule 43 or Rule 22 of the Federal Rules of Civil Procedure."

But the fact is that, although the *Liverpool* case grew out of a garnishment proceeding, both the Fifth Circuit (209 F. 2d 684, 686) and this Court (p. 216) regarded it an "interpleader action." Moreover, in *Liverpool* as here, the "interpleader action" had been removed from a Texas state court to a United States District Court (*ibid.*). In *Liverpool,* this Court concluded (p. 217) that "* * * certainly fees allowed in that proceeding are not prior to the Government liens, and the authorization of the payment of the attorney's fees prior to the Government liens was error."

That holding would appear to be fully dispositive here.[20]

---

[20] The case of *United States* v. *Ullman*, 115 F. Supp. 241 (E. D. Pa.), which the court below followed, was decided prior to this Court's decision in the *Liverpool* case. Moreover, the *Ullman* case is not "directly in point," as was held below (R. 14), since there the United States had instituted the suit to foreclose its income tax liens. The *Ullman* case is distinguished in *Ford Motor Co.* v. *Hackart Construction Co.*, 143 F. Supp. 216 (N. J.), where it is pointed out that the decision in the *Ullman* case did not purport to resolve a conflict between a government lien and an allowance of fees since the question of priorities of interest in the interpleaded fund had not been reached. The decision of this Court in the *Liverpool* case was also followed in *Bruce* v. *United States*, 127 F. Supp. 858 (E. D. Mich.), and *Boston Insurance Co.* v. *Stubbs* (W. D. Wash.), decided March 20, 1956 (1956 C. C. H., par. 9695).

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment below should be reversed.

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SEPTEMBER 1957.

APPENDIX

Internal Revenue Code of 1939:

SEC. 3670. PROPERTY SUBJECT TO LIEN.

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, additional amount, or addition to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

(26 U. S. C., 1952 ed., Sec. 3670.)

SEC. 3671. PERIOD OF LIEN.

Unless another date is specifically fixed by law, the lien shall arise at the time the assessment list was received by the collector and shall continue until the liability for such amount is satisfied or becomes unenforceable by reason of lapse of time.

(26 U. S. C., 1952 ed., Sec. 3671.)

SEC. 3672 [as amended by Sec. 401 of the Revenue Act of 1939, c. 247, 53 Stat. 862, and Sec. 505 of the Revenue Act of 1942, c. 619, 56 Stat. 798]. VALIDITY AGAINST MORTGAGEES, PLEDGEES, PURCHASERS, AND JUDGMENT CREDITORS.

(a) *Invalidity of Lien without Notice:*—Such lien shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the collector—

(1) *Under state or territorial laws.*—In the office in which the filing of such notice is authorized by the law of the State or Territory in which the property subject to the lien is

situated, whenever the State or Territory has by law authorized the filing of such notice in an office with the State or Territory; or

* * * * *

(26 U. S. C., 1952 ed., Sec. 3672 (a).)

1 Vernon's Civil Statutes of the State of Texas, Annotated:

ART. 260–1. *Accounts and accounts receivable; notices; records*

SECTION 1. Definitions: In this Act, unless the context otherwise requires:

(1) "Account" or "account receivable" means an existing or future right to the payment of money presently due, or to become due (a) under an existing contract: * * *

* * * * *

(4) "Assignment" means any transfer of an account, other than by operation of law, including but not limited to a transfer as security, the creation by agreement of a lien on an account, and sales of accounts.

SEC. 2. The assignment of any account or accounts may be protected by the execution and delivery by the assignor to the assignee of an instrument or instruments in writing, assigning such account or accounts and describing the account or accounts assigned with sufficient particularity to identify the same, and by the filing for record the "Notice of Assignment" as hereinafter provided for.

* * * * *

SEC. 6. Whenever any person, firm or corporation shall in good faith take a protected assignment of any account or accounts, which shall not have been satisfied, cancelled or released by the assignor, all creditors of, and all subsequent assignees, purchasers and transferees of or from the assignor shall be conclusively deemed to have received notice of such assignment, dating from the time of the filing

for record of the notice of assignment hereinabove provided; and after such filing for record, no purchaser from the assignor, no creditor of any kind of the assignor, and no prior or subsequent assignee or transferee of the assignor, holding an assignment not protected, or holding an assignment under a notice of assignment subsequently filed for record, shall in any event have, or be deemed to have acquired, any right in the account or accounts so assigned or in the proceeds thereof, or in any obligation substituted therefor, superior to the rights therein of the assignee named in such prior protected assignment.

* * * * *

Acts 1945, 49th Leg., p. 463, ch. 293.

16 Vernon's Civil Statutes of the State of Texas, Annotated:

ART. 5490. *Chattel mortgages*

Every chattel mortgage, deed of trust, or other instrument of writing, intended to operate as a mortgage, or lien upon personal property, and every transfer thereof which shall not be accompanied by an immediate delivery and be followed by an actual and continued change of possession of the property mortgaged, pledged, or affected by such instrument, shall be absolutely void as against the creditors of the mortgagor or person making same, as against subsequent purchasers and mortgagees or lien holders in good faith, unless such instrument, or a true copy thereof, shall be forthwith deposited with and filed in the office of the county clerk of the county where the property shall then be situated, or if the mortgagor or person making the same be a resident of this State, then, of the county of which he shall at that time be a resident; * * *.

Acts 1925, 39th Leg., p. 368, ch. 157.

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No. 97

UNITED STATES OF AMERICA,

PETITIONER

vs.

R. F. BALL CONSTRUCTION COMPANY, INC., and
UNITED PACIFIC INSURANCE COMPANY,

RESPONDENTS

Reply of United Pacific Insurance Company to Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

No. 880

UNITED STATES OF AMERICA,
PETITIONER

vs.

R. F. BALL CONSTRUCTION COMPANY, INC., and
UNITED PACIFIC INSURANCE COMPANY,
RESPONDENTS

Reply of United Pacific Insurance Company to Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

---

The Respondent, United Pacific Insurance Company, in reply to the above styled petition for certiorari to the United States Court of Appeals for the Fifth Circuit says:

I.

The statement by Petitioner of the facts is substantially correct but the statement of the first question presented is misleading. The first "question presented" should be stated as follows:

> "Whether an indemnity mortgagee, namely a surety who takes collateral security to protect is against future contingent loss, comes within the term **'Any* mortgagee'** as used in Section 3672 of the Internal Revenue Code of 1939, which in effect subordinates federal tax liens to a prior lien of **'any mortgagee'**."

Petitioner, in support of its misleading statement of the first question, on page 10 of its petition says:

> "* * * in order to qualify as a 'mortgage' (or 'pledge') for purposes of Section 3672, surely an assignment to secure an indebtedness must—at the very least—relate to an **existing**** indebtedness, not merely an indebtedness that might arise in the future."

Petitioner cites no authority for this sweeping statement. We say, without fear of successful contradiction, that the reason the Petitioner cites no authority for this broad statement is that not only is there no authority to be found to support it but ample authorities are to be found directly to the contrary.

The indemnity mortgage in this instance was given to secure the surety on its contingent liability. More than 150 years ago, John Marshall, that great chief justice of the United States, in the case of **U. S. vs. Hooie,** 3 Cranch 73, 2. L.Ed. 370, upheld what are known in law as "indemnity mortgages". There, one Hooie went surety on a bond for one Fitzgerald to the United States and took an indemnity mortgage as security. In a contest of priorities between the United States and the surety, Chief Justice Marshall said:

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*Here, and throughout this brief, unless otherwise stated, the emphasis is supplied.

**Emphasis is the Petitioner's.

"The deed is made to save Hooie harmless on account of his having become the security of Fitzgerald to the United States * * *. All the covenants in the deed apppear to the court to be fair, legitimate and consistent with common usage."

The court then went on to uphold the mortgage to secure this contingent liability of the surety.

Such was likewise the situation in the very early Texas case of **Williams vs. Silliman,** 74 Tex. 626, 12 S.W. 534, where the Supreme Court of Texas upheld an indemnity mortgage to a surety in a very brief opinion which closed with the statement:

"The desire to indemnify his security against loss was a sufficient consideration for the execution of the mortgages."

41 **Corpus Juris,** 459 states as follows:

"D. INDEMNITY MORTGAGES — 1. VALIDITY IN GENERAL. It is well settled that a mortgage given by way of indemnity, that is, not founded on a present debt, but meant to secure the mortgagee against loss or damage in consequence of a contingent liability or responsibility which he has assumed or agreed to assume for and on behalf of the mortgagor, as surety, bail, indorser, or otherwise, is valid and enforceable.

"FUTURE LIABILITIES. An indemnity mortgage may be given to secure the mortgagee not only as against debts or liabilities for which he has already assumed responsibility or liability, but also to protect him against loss or damage on indorsements, suretyships, or other liabilities which he may in the future enter into for the benefit of mortgagor."

Many authorities from the various states are cited in support of these statements.

The same authority, on page 528, in discussing priorities of an indemnity mortgage, says:

> "A mortgage given to indemnify the mortgagee or to secure him against a secondary or contingent liability, such as that of an indorser or surety, may take precedence over liens created subsequent to its execution * * *."

On this same subject, 36 **Am. Jur.** 720, has the following to say:

> "A mortgage need not be founded on a present debt, but may be given to secure the performance of other obligations. The mortgage may be made to secure future advances or to indemnify against a contingency which may in fact never occur. It may be given to secure one as an indorser or as a surety upon a bond. The security of a mortgage given to indemnify sureties has been held not to be limited to the nominal money consideration recited, but to extend to the amount for which the sureties ultimately prove liable."

Similar statements are found in 59 C.J.S. 138 and 215.

It is submitted that Petitioner's statement of the law above quoted is wholly at variance with all of the authorities on the subject of indemnity mortgages.

Petitioner likewise on page 10 makes the statement, which is wholly unsupported by anything in the record, that "the indebtedness secured by the assignment did not come into existence until long after the federal liens were perfected." The obligation of the surety

came into existence on April 4, 1952, as found by the trial court (P. 16)* and as was stipulated (R. 8), which was more than a year prior to the fixing of the tax liens. It is true that the obligation which was assumed by the surety on April 4, 1952, was not discharged until after the filing of the tax liens in question, but nowhere in this record is there to be found either a stipulation or a finding or any evidence that the indebtedness of the surety "did not come into existence until long after the federal liens were perfected," as stated by petitioner. The precise time when it became known that there would be a loss on this bond is not to be found in the record. The only finding and stipulation being that the surety's obligation to pay was assumed more than a year prior to the fixing of the tax liens but was not actually paid until after the fixing of the tax liens. The payment after the filing of the tax liens was not a voluntary payment but the surety, as found by the trial court (R. 13) "was required to pay by virtue of its bond in connection with the Kentucky project, the sum of $12,971.88."

Suppose Jacobs, the taxpayer principal in this case, instead of giving an assignment of the retained percentages under the San Antonio contract as security to protect the surety on its contingent liability, had given a deed of trust on certain lands to the surety at the time it executed its Kentucky bond. Under all of the authorities heretofore cited, such a deed of trust (even though not technically denominated "a mortgage") would have been prior to any other claims arising thereafter. Can there be any substantial difference between a "deed of trust" and an "assignment as

*Throughout this Reply. "P." will refer to the page of the Petition for certiorari and "R." will refer to the page of the Record in the Court of Appeals.

collateral security"? Certainly no such distinction is apparent.

It is submitted that this Respondent's statement of the first Question Presented is an accurate statement and that the surety being an indemnity mortgagee is protected by Section 3672 as coming within the term "**any** mortgagee [or] pledgee."

II.

Under the heading "Reasons for Granting the Writ" (P. 6) the Petitioner gives four reasons why it claims this court should grant the Writ of Certiorari.

First, Petitioner says "the decision below is in direct conflict with the decisions of this court holding that the relative priority of a federal tax lien is a federal question." Petitioner has misconstrued the position of this Respondent and the courts below. This Respondent admits and neither of the courts below denied that the relative priority of a federal tax lien is a federal question. It is Hornbook law that the construction of a federal statute is a federal question.

Second, the Petitioner says that "the classes of lienors ("mortgagee, pledge [sic], purchaser, or judgment creditor) protected by Section 3672 of the Internal Revenue Code of 1939 (**supra**, p. 3) are to be defined in the usual and conventional sense of the terms."

Just what Petitioner claims to be the "usual and conventional" sense of the terms "mortgagee" and "pledgee" the Petitioner does not enlighten us by giving a definition, nor does Petitioner point out wherein an "indemnity mortgagee" does not come within the category of "**any** mortgagee (or) pledgee".

More than a century and a quarter ago this court in the case of **Conard vs. Atlantic Ins. Co.,** 1 Peters 386 at 441, 26 U. S. 189 at 213, said in defining the term "mortgage":

> "It is true that in discussions in courts of equity a mortgage is sometimes called a lien for debt. And so it certainly is and something more; it is a transfer of the property itself as security for the debt. This must be admitted to be true at law. * * *"

This court likewise at an early date in the case of **Willamette etc. vs. Bank of British Columbia,** 119 U. S. 191, defined a mortgage as follows:

> "A mortgage is in effect a sale with a power of defeasance which may ultimately end in an absolute transfer of title."

The property interests of the surety and the principal in this transaction, however, were not created by federal law. As was said by Judge Medina on February 8, 1957, in speaking for the Court of Appeals for the Second Circuit in the case of **Fidelity & Deposit Co. of N. Y. vs. N. Y. City Housing Authority, et al,** 241 F. 2d 142.

> "Section 3670 imposes a tax lien on 'all property and rights to property' of a defaulting taxpayer. In adopting this legislation, the Congress did not create property interests on which a lien might be imposed; there is no suggestion that it authorized the federal courts to do so. On the contrary, it took for granted here, as it normally does in the tax law, the vital existence of the state laws creating and maintaining various interests. The statute was fashioned to require the courts to determine for federal purposes whether those state-created interests are 'prop-

erty' or 'rights to property.' That classification of interests is a federal question; the existence of the interests to be federally classified, however, is solely a question of state law.

"This distinction was formulated by the Supreme Court in Morgan v. Commissioner, 309 U. S. 78, 80, which also involved the tax law. 'State law', the court explained, 'creates legal interests and rights. The federal revenue acts designate what interests or rights, so created, shall be taxed. Our duty is to ascertain the meaning of the words used to specify the thing taxed. If it is found in a given case that an interest or right created by local law was the object to be taxed, the federal law must prevail no matter what name is given to the interest or right by state law.' "

Turning then to the law of the state which created this interest, 29 **Tex. Jur.** 736 says:

"A mortgage in the broadest sense of the term is a pledge of property either real or personal or of a chose in action, as security for the performance of an obligation which ordinarily consists in the payment of money. In the language of Chancellor Kent, a mortgage is 'a conveyance of an estate or property by way of pledge for the security of a debt to become void on payment of it.' "

The courts below likewise cited 29 **Tex. Jur.** 838 wherein it is said:

"A mortgage which purports to secure future debts is not ineffectual or invalid. On the contrary, the lien created will be enforced, not only in a dispute between the mortgagor and mortgagee, but **also in a controversy involving the rights of one who claims under the mortgagor.**"

Of course, Petitioner is here claiming under the mortgagor because under Section 3670 the Petitioner's lien reaches only "*** property and rights to property whether real or personal belonging to" the mortgagor in this instance.

It is submitted that the surety in this case, being an indemnity mortgagee (or pledgee), came within the "usual" and "conventional" sense of the terms "any mortgagee [or] pledgee" within the meaning of Section 3672.

Petitioner gives as its third reason why this court should grant Certiorari the claimed fact that the decision below is in direct conflict with the decisions of this court holding "that the federal tax lien provided by Section 3670 (**supra**, p. 2) is entitled to priority as against inchoate liens not specifically protected by Section 3672". This is likewise an incorrect statement from two standpoints. First, this court has never held that a federal tax lien is superior to a mortgage (or pledge) merely because the debt secured by the mortgage (or pledge) was not due or was an indemnity mortgage or was not in an amount certain. Second, the courts below recognized that there are certain classes of liens, all of which are statutory in character, such as an attachment, garnishment, statutory landlord's, water rent, and other liens which, since they are not specifically protected by Section 3672, are inferior unless such liens are "choate". (For an interesting discussion of this court's coining of the word "choate" which term is not to be found in any ordinary dictionary see 42 Am. Bar Ass'n. Journal 608, July 1956). The decisions of this court using the term "choate" all have to do with the fourth category in Section 3672, to-wit: "judgment creditors", and this court has held that before one can come within the category of a "judgment

creditor" his judgment lien must be "choate" in the sense that it is perfected and complete. Never has this court, or any other court for that matter, finally determined that a mortgage (or pledge) must be "choate" in order to be protected under Section 3672.

Attention is called to the fact that in the vast majority of mortgages, pledges, or other contract liens, it cannot be determined at the time of the execution thereof how much of the mortgaged or pledged property or fund will have to be used for the payment of the secured debt. In most instances today the mortgagor pays off the debt secured by the mortgage and when this happens there is no need to resort to the pledged or mortgaged fund or property. In other pledges or mortgages, the pledgor or mortgagor pays off part of the debt. Furthermore, in most instances, the pledgor or mortgagor has the privilege which it sometimes exercises by paying it in advance, thereby reducing the amount of interest. Furthermore, in most mortgages or pledges, attorneys fees upon default are provided for and, of course, at the time of the execution of the mortgage it cannot be ascertained whether or not attorneys fees will be added to the amount of the mortgaged debt nor how much interest will be due and payable ultimately out of the pledged or mortgaged fund or property.

It is obvious, therefore, that practically no mortgage today is complete or "choate" at the time the pledge or mortgage is made. Such was definitely the case in connection with the commissions to be earned by the creditor "when they shall become available to him" in the case of **National Refining Company vs. U. S.** 160 F 2d 951, since at the time of the assignment no commissions had accrued to the creditor and it was possible that no commissions would ever be earned.

Likewise the assignment of future wages in the case of **Knight vs. Knight,** 71 N. Y. Sup. 2d 357, affirmed by the court of last resort of New York, 80 N. E. 2d 344, was not complete or "choate" at the time it was given because the wages at that time had not been earned and such wages might never have been earned.

The amount of what ultimately would be the retained percentages under the assignment thereof was equally uncertain in **Northern Nat. Bank vs. Northern Minn. Nat. Bank,** 70 N. W. 2d 118 and in **U. S. F. & G. vs. U. S.** 20 Fed 2d 118. Just as was the extent of the property assigned in the case of **U. S. vs. Gargill,** 218 Fed. 2d 556.

In all these instances, the courts held that the assignments, or mortgages, or pledges, were superior to the subsequently filed tax liens. Many other similar instances could be cited.

As its fourth reason why this court should grant the writ, Petitioner claims that the decision below is in conflict with the decisions of this court holding that "the doctrine of relation back cannot operate to destroy the realities of the situation."

This Respondent did not urge upon the courts below the equitable doctrine of relation back and the courts below did not decide this case on any such doctrine. The courts below held that the surety being an indemnity mortgagee (or pledgee) within the meaning of Section 3672 was protected and there was no occasion to resort to the equitable doctrine of relation back.

All of the authorities relied upon by petitioner are cited on pages 6 and 7 of the petition for Writ of Certiorari. As stated above, all of these authorities have to do with the construction of the term "judgment creditor" as contained in Section 3672. None of them even

purport to deal with the terms "**any** mortgagee [or] pledgee". Petitioner, however, states (P. 11) in effect that these cases lay down the broad "rule" that a perfected federal tax lien is entitled to priority as against an "inchoate lien" even though the inchoate lien may be a mortgage, pledge, or other contract right entered into long prior to the perfecting of the tax lien. The decisions of this court do not support any such assertion, as will be demonstrated.

It will be recalled that in the Internal Revenue Act of 1939, Title 26, U.S.C., Section 3672, it is provided that a subsequently filed federal tax lien "shall not be valid as against **any** mortgagee, pledgee, purchaser, judgment creditor, etc."

In the case of **U. S. vs. Security Trust & Savings Bank,** 340 U.S. 47 (1950) this court held that an attachment lien in California which had not ripened into a final judgment so as to make the holder of such lien a "judgment creditor" was inferior to a federal tax lien which was filed after the attachment lien was levied but before the judgment became final, since mere attachment liens as such were not protected specifically under Sec. 3672.

Thereafter this court in 1953 in the case of **U. S. vs. Gilbert & Associates,** 345 U.S. 361, held that a municipality holding a tax lien for municipal taxes against certain properties was not a "judgment creditor" within the meaning of Section 3672 and that the federal tax lien was superior to the municipal tax lien which was not specifically protected by Section 3672.

Thereafter in 1954 this court handed down its decision in the case of **U. S. vs. City of New Britain,** 347 U.S. 81 in which it held that a lien for municipal taxes and statutory water rent liens which had not

ripened into judgment at the time of the filing of the federal tax lien were subordinate to a federal tax lien since they were not protected by Section 3672.

Thereafter on January 10, 1955, this court handed down its decisions in the cases of **U. S. vs. Acri,** 348 U.S. 211, **U. S. vs. Liverpool, etc. Ins. Co.,** 348 U.S. 215, and **U. S. vs. Scovil,** 348 U.S. 218.

In the **Acri** case this court held that the holder of an attachment lien similar to the attachment lien in the **Security Trust & Savings Bank** case, supra, until the judgment became final did not come within the term "judgment creditor" and therefore was not protected under Section 3672.

In the **Liverpool** case this court held that the holder of a garnishment lien before final judgment was not a "judgment creditor" within the meaning of Section 3672, and in the **Scovil** case this court held that the holder of a statutory landlord's lien prior to the time the same ripened into a final judgment was not a "judgment creditor" within the meaning of Section 3672.

Summary reversals were made by this court in the cases of **U. S. vs. Colotta,** 350 U.S. 808, and **U. S. vs. White Bear Brewing Co.,** 370 U.S. 1010, relative to unperfected statutory mechanics liens which had not ripened into final judgments and therefore were not protected under Section 3672. Such was also the holding of the Court of Appeals of the Second Circuit in the case of **U. S. vs. Kings County Iron Works,** 224 Fed. 2d 232.

All of the above cases which are relied upon by Petitioner were constructions of the term "judgment creditor" under Section 3672. None of these cases undertook to construe or discuss contractual rights

such as indemnity mortgages (or pledges), or assignments such as the one involved in the case at bar but Petitioner now says that "there is no basis for assuming that Congress in enacting Section 3672 intended different priority standards to apply to the designated non-statutory liens and statutory liens" (P. 11) or, as Petitioner said in the courts below, "the principles of **U. S. v. Security Trust & Savings Bank, U. S. v. New Britain, U. S. v. Scovil, U. S. v. Acri,** and **U. S. v. Liverpool & London Ins. Co.,** supra, must be applied." (R. 15, P. 19).

As was stated by the courts below (P. 22) "The distinction between a contract lien and a statutory lien is made clear by comparing the case of **Evans vs. Stewart,** (66 N. W. 2d 442) with the **Scovil** case, supra. In the **Scovil** case, the Supreme Court held that prior to the time it ripened into a final judgment an incompleted statutory landlord's lien was inferior to a federal tax lien since the holder thereof was neither a 'mortgagee,' 'pledgee,' 'purchaser,' nor 'judgment creditor.' In the **Evans** case, the court held that a written contract landlord's lien contained in the lease was superior to a federal tax lien because it was a 'mortgage' within 3672."

The Petitioner argued in the courts below and inferentially argues here that because the parties to the indemnity mortgage involved here did not place the label on the transaction of the surety becoming a "mortgagee," "pledgee," or "purchaser," its contract right acquired long prior to the filing of the tax lien must fail, but as stated by the courts below "courts do not decide cases on nomenclature. They look to the substance of the transaction and the substance of the assignment here was to put the bonding company

in the status of either a mortgagee, pledgee, or purchaser and, therefor, Section 3672 applies."

This court recently said in the case of **Cahill vs. N. Y. N. H. & H. Ry. Co.**, 351 U.S. 183:

> "The substance of the pleadings and not their labels should govern our actions."

So here the substance of the transaction between the surety and the principal and not the label should govern this court's action.

As stated above, Petitioner says that "there is no basis for assuming that Congress in enacting Section 3672 intended different priority standards to apply to the designated non-statutory liens than to statutory liens." With this statement we take issue. There is good basis for assuming just to the contrary.

After all the problem before this court is to determine what the Congress had in mind when in Section 3672 it used the terms "**any** mortgagee [or] pledgee" and the use of the word "**any**" gives a clear indication of the congressional intent. In 1954 Congress was in the process of completely revamping the Internal Revenue Code and it had before it the question as to whether or not Section 3672 of the 1939 Code should be amended. Appendix A to this brief is the complete report of the Committee on Ways and Means in the House of Representatives and Appendix B hereto is the report of the Committee on Finance of the United States Senate having to do solely with amending Section 3672. It will be noted that in the House report it was suggested that just who is "**any** mortgagee [or] pledgee" should be spelled out and in explanation of this suggestion the Committee report says:

> "'This subsection is not designed to extend the protection of subsection (a) of this section to

categories of persons now denied protection by existing court decisions (under Section 3672(a) of the 1939 code) which determine who is a mortgagee, pledgee, purchaser, or judgment creditor by reference to **the realities and the facts in a given case rather than to the technical form or terminology used to designate such person.**"

The Senate report rejected the House proposal as being unnecessary and with the subsequent concurrence of the House Section 3672 was left intact because, as said by the Senate report:

"Subsection (c) of the House bill provided certain rules with respect to the validity of the tax lien, without the filing of notice thereof, as against mortgagees, pledgees, purchasers, or judgment creditors. The applicable rules have been developed under existing law by judicial construction, and your committee deems it advisable to continue to rely upon judicial interpretation of existing law instead of attempting to prescribe specific statutory rules. The deletion of subsection (c) will continue in effect the existing law.

"This section corresponds to section 3672 of the 1939 Code. **As under existing law, a person who is in fact a mortgagee, pledgee, purchaser, or judgment creditor will be entitled as such to the protection of this section irrespective of the designation applied to such person under State law,** for example, in a State which has adopted the Uniform Commercial Code and which uses other terms to describe such persons."

In other words, in 1954 Congress was satisfied with the then court decisions construing the term "any mortgagee, etc." to the effect that regardless of the

label placed on a contract lien creditor if he was "in fact a mortgagee, (or pledgee)" he would be protected and Congress was likewise satisfied with the existing court decisions which determined who is any mortgagee or pledgee "by reference to the realities of the facts in a given case rather than the technical form or terminology used to designate such persons."

What were these decisions that Congress was satisfied with? They were the very decisions now relied upon by this Respondent in this case, such as **Knight vs. Knight**, supra, **National Refining Co. vs. U. S.** supra, **U. S. vs. Anders Contracting Co.**, 111 Fed. Sup. 70 and the other cases heretofore referred. Is there any reason in justice why an "assignment as collateral security" should not be protected as coming within the term "**any** mortgagee" but the holder of a "deed of trust" or "conditional sales contract" or an "assignment of future wages" or "an assignment of future commissions" should. We submit not. But that is exactly what the Petitioner is contending for in this case unless Petitioner is seeking to have this court overturn all of the above decisions with which Congress was satisfied in 1954.

In the case of **Evans vs. Stewart**, supra, in discussing Section 3672 the Supreme Court of Iowa held in line with the above expressed intent of the Congress that:

> "We feel the requirement that the lien holder be a 'mortgagee' is a requirement of status—that he be in the position of one holding a mortgage."

Such was also the holding of the United States Court of Appeals for the First Circuit in the case of **U. S. vs. Gargill**, supra, where the court in construing Section 3672 said:

> "If the three trustees named in the agreement of February 19, 1952 acquired the status of 'mortgagee' because of the transaction occurring on that date and this prior to the filing of the notice of the tax lien by the collector on June 24, 1952, their lien is senior and is to be preferred over the lien of the Government."

The unpublished opinion of the trial court in the **Gargill** case seems pertinent wherein the trial court in construing Section 3672 said:

> "It seems to me plain that it was the intention of Congress that a mortgage or pledge of any sort should be given priority over an unrecorded tax lien. **It makes no difference whether the mortgage corresponds to the ancient English form or some other form.** It makes no difference whether it is to secure antecedent debt or newly acquired debt. It makes no difference whether the mortgagee is left in possession or not left in possession. **The only thing which is required is that the transaction be such that the person or persons claiming to have the mortgage shall have that kind of security which involves either a transfer of title or a lien which is of a nature that gives the holder a right in rem with respect to the property and privilege to precede unsecured creditors. The phrases used in the statute were not used with some medieval notion of mortgage, pledge or the like. The whole object of the Congressional legislation is not to resurrect a page of Year Book history but to give that protection which persons in a modern world associate with the security they have achieved as a result of their diligence and forethought."**

The statements above quoted from the **Gargill** case are borne out by Mr. Justice Jackson's concurring opinion in the case of **U.S. vs. Security Trust & Savings**

Bank, supra. Justice Jackson there goes into the legislative history of Section 3672 and he points out that when this Section was adopted in 1939 the Congress itself stated that its intention was to prevent federal tax liens from seriously interfering with "business transactions." For this court to do what Petitioner urges would "seriously interfere with business transactions." As pointed out heretofore, practically no mortgage in existence today is "choate" in the sense that it is a thing complete. Furthermore, the security of the retained percentages taken by assignment or indemnity mortgage by sureties in construction bonds are taken into consideration in fixing the premiums on construction bonds and if this security be denied the premiums on construction bonds will have to be increased and it will be much more difficult for a small contractor, or in some instances even a large one, to secure sureties on their construction bonds. It can readily be seen that a holding by this court such as Petitioner urges would "seriously interfere with business transactions" which is the thing that Congress has avidly guarded against.

The Petitioner in this case says (P. 11):

> "In this case the **advances** for which the bonding company seeks 'mortgagee' status were not made for several months after the federal liens had been recorded."

Just why the Petitioner should use the word "advances" in describing the payment made by the surety on an obligation which it assumed long prior to the filing of the tax lien is not clear unless it is for the purpose of misleading this court. Webster defines the term "advance":

> "To furnish, as money or other value, before it is due, in aid of an enterprise; to supply beforehand."

Of course the surety here did not "advance" any money. It merely discharged an obligation incurred long prior to the filing of the tax liens.

Had this been a voluntary "advance" by the surety then such decisions as **U.S. vs. Phillips,** 198 F. 2d 634 might be applicable but as found by the trial court the payment by the surety was not an "advance" in any sense of the word but was a payment which the surety "was required" to make by virtue of the obligation assumed more than a year prior to the filing of the tax lien.

Petitioner further says: (P. 11)

> "Prior to the recording of the federal liens, there was at most a mere possibility that the taxpayer might become indebted to the bonding company. Such a mere possibility is plainly insufficient to constitute a specific and choate lien under this court's decisions. (**supra**). For like reasons, such a mere possibility is insufficient to entitle the bonding company to the status of a mortgagee under Section 3672."

Indemnity mortgages are intended as security against just such possibilities. The Petitioner cites no authority for this broad statement and again we say that no authority in support thereof can be found but ample authorities to the contrary have heretofore been cited by this respondent to the court.

Petitioner further says: (P. 11)

> "And even assuming **arguendo*** that the 1951 assignment matured into a 'mortgage' (or 'pledge') in December 1953 and March 1954

*Emphasis Petitioner's.

when the bonding company made its **advances***, this court's decisions have also made it clear that the doctrine of relation back will not be permitted to destroy the realities of the situation."

This respondent is not contending that its indemnity mortgage "matured" when it made its payments. It is contending that its indemnity mortgage arose and became effective at the time it was given, for as stated in the case of **Hawkins vs. Savage,** 110 F. Sup. 615:

> "A lien 'arises' at the time it comes into being or is created."

The indemnity mortgage of the surety in this instance came into being and was created in 1951, approximately two years prior to the filing of any tax liens. Again the Petitioner incorrectly uses the term "advance" to describe the payments which were required to be made by the surety because of an obligation which it assumed a year before any tax liens were filed and as this respondent has stated before, this respondent is not relying and has never relied in this case on the equitable doctrine of relation back.

It is, therefore, submitted that none of the four reasons given by Petitioner as to why this court should grant certiorari in this case is tenable.

III.

Although this Respondent is not pecuniarily interested in the subsidiary question presented of whether or not interpleaders' attorneys' fees can be allowed as against the Petitioner, this Respondent is interested

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*Emphasis Petitioner's.

in a speedy disposition of this matter so that the money which has been lying in the registry of the court for approximately three years without interest, may be drawn down and put to use. This Respondent believes that the lower courts were correct in holding in line with the decision in **U.S. vs. Ullman,** 115 F. Sup. 211, that such interpleaders' fee should be allowed and the Court of Appeals for the Fifth Circuit in this case is the first Court of Appeals to pass upon this question.

Only the sum of $256.67 is involved in this matter so that actually the doctrine of **de minimus non curat lex** could well be applicable. However, should this court feel that the courts below were in error in depriving Petitioner of this less than $256.67 in this multi-thousand dollar suit, it is suggested that certiorari be granted and only that portion of the judgments of the lower courts having to do with attorneys fees against Petitioner be summarily reversed so that this Respondent will not be deprived of its money any longer.

SUMMARY OF ARGUMENT AND CONCLUSION

The judgments of the lower courts in this case were correct. This Respondent being an indemnity mortgagee whose contract right vested long prior to the filing of any federal tax liens, has the superior right to the funds in the registry of the court and the petition for certiorari should be denied.

In the alternative, should this court feel that the lower courts erred only in connection with the award of attorneys fees to the Petitioner's prejudice of only $256.67, this court should summarily reverse only that

portion of the lower courts' judgment having to do with attorneys' fees and affirm as to the surety.

Respectfully submitted,

Jack C. Hebdon

JACK C. HEBDON
Attorney for Respondent
United Pacific Insurance Company

OF COUNSEL:
JOSH H. GROCE

I hereby certify that on the 18th day of April, 1957, I deposited in a U.S. Mail box with air mail postage prepaid, three copies of the foregoing reply directed to the Solicitor General, Department of Justice, Washington 25, D.C. in compliance with Supreme Court Rule 33 and I further certify that on the same date I deposited in a U.S. Mail box three copies of this reply directed to Richard U. Simon, Oil & Gas Building, Fort Worth 2, Texas, Attorney for R. F. Ball Construction Company, Co-Respondent, with first class postage prepaid.

APPENDIX A

EXCERPT FROM REPORT OF THE COMMITTEE ON WAYS AND MEANS, HOUSE OF REPRESENTATIVES, TO ACCOMPANY H.R. 8300—HOUSE REPORT NO. 1337, DATED MARCH 9, 1954. 83rd CONGRESS. UNITED STATES GOVERNMENT PRINTING OFFICE. Page A406

Section 6323. **Validity against mortgagees, pledgees, purchasers, and judgment creditors**

This section corresponds to section 3672 of the 1939 code. Subsection (b) makes it clear that the notice of lien shall be valid, notwithstanding any law of the State or Territory regarding the form or content of a notice of lien, if the notice is in such form as would be valid if filed with the clerk of the United States district court pursuant to subsection (a) (2) of this section. The Treasury Department has consistently taken the position that section 3672 of the 1939 code and the corresponding provisions of prior law authorize the State or Territory only to designate the local office for the filing of the notice of the lien. Subsection (b) is designed to eliminate any question as to the validity of the lien as against mortgagees, pledgees, purchasers, and judgment creditors, where notice thereof is filed in the office designated by the law of the appropriate State or Territory, even though the notice does not comply with other requirements of the law of the State or Territory as to the form or content of the notice. For example, the omission from the notice of lien of a description of the property subject to the lien would not affect the validity thereof, even though the law of the State or Territory requires that the notice of lien contain a description of the property subject

to the lien. Subsection (b) of this section is declaratory of the existing procedure and in accordance with the long-continued practice of the Treasury Department.

Subsection (c) makes it clear that the protection of subsection (a) of this section is not extended to a mortgagee, pledgee, or purchaser who takes with notice or knowledge of the existence of the Federal lien; and that such protection is not extended to a judgment creditor who does not have a valid judgment obtained in a court of record and of competent jurisdiction or to a judgment creditor who does not have a lien which has been properly perfected under such a judgment. This subsection is not designed to extend the protection of subsection (a) of this section to categories of persons now denied protection by existing court decisions (under section 3672 (a) of the 1939 code) which determine who is a mortgagee, pledgee, purchaser, or judgment creditor by reference to the realities and the facts in a given case rather than to the technical form or terminology used to designate such person. Paragraph (1) of subsection (c) provides that the lien shall be valid, without the filing of notice thereof, as against any mortgagee, pledgee or purchaser, if such mortgagee, pledgee, or purchaser had notice of knowledge of the existence of the lien at the time the mortgage, pledge, or purchase, was made. A dual requirement is set forth in paragraphs (2) and (3) of this subsection which a judgment creditor must meet to be entitled to the protection of the notice provisions of subsection (a) of this section. One requirement is that the judgment creditor must have actually obtained a valid judgment in a court of record and of competent jurisdiction for the recovery of specifically designated property or for a certain sum of money; and the other requirement is that the judgment creditor, in the case

of a valid judgment for the recovery of a certain sum of money, must have a perfected lien under such judgment on the property as to which the claims of the contesting parties relate. Furthermore, subsection (c) makes clear that particular persons shall not be treated as judgment creditors because State or Federal law artificially provides or concedes such persons rights or privileges of judgment creditors, or even designates them as such, when they have not actually obtained a judgment in the conventional sense.

Subsection (d) of this section is in all material respects the same as existing law.

Subsection (e) of this section makes it clear that the Secretary may, after a notice of lien has been filed (and such notice discloses the amount of the outstanding liability as of the time of filing), disclose the extent to which the original obligation has been reduced by subsequent payments. This is necessary for the protection of persons dealing with property subject to the lien who have a legitimate interest in determining the amount of the outstanding obligation, as well as to aid reestablishment of the taxpayer's credit.

APPENDIX B

EXCERPT FROM REPORT OF THE COMMITTEE ON FINANCE, UNITED STATES SENATE, TO ACCOMPANY H.R. 8300—UNION CALENDAR NO. 1635, DATED JUNE 18, 1954. 83rd CONGRESS. REPORT NO. 1622, PRINTED IN THE U.S. GOVERNMENT PRINTING OFFICE, Page 575

Section 6323. **Validity against mortgagees, pledgees, purchasers and judgment creditors**

This section corresponds to that of the House bill except for the deletion of subsection (c) of the House bill and conforming changes incident to such deletion.

Subsection (c) of the House bill provided certain rules with respect to the validity of the tax lien, without the filing of notice thereof, as against mortgagees, pledgees, purchasers, or judgment creditors. The applicable rules have been developed under existing law by judicial construction, and your committee deems it advisable to continue to rely upon judicial interpretation of existing law instead of attempting to prescribe specific statutory rules. The deletion of subsection (c) will continue in effect the existing law.

This section corresponds to section 3672 of the 1939 Code. As under existing law, a person who is in fact a mortgagee, pledgee, purchaser, or judgment creditor will be entitled as such to the protection of this section irrespective of the designation applied to such person under State law, for example, in a State which has adopted the Uniform Commercial Code and which uses other terms to describe such persons.

Subsection (b) of this section makes it clear that the notice of lien shall be valid, notwithstanding any law of the State or Territory regarding the form or content of a notice of lien, if the notice is in such form as would be valid if filed with the clerk of the United States district court pursuant to subsection (a) (2) of this section. The Treasury Department has consistently taken the position that section 3672 of the 1939 Code and the corresponding provisions of prior law authorize the State or Territory only to designate the local office for the filing of the notice of the lien. Subsection (b) is designed to eliminate any question as to the validity of the lien as against mortgagees, pledgees, purchasers, and judgment creditors, where notice thereof is filed in the office designated by the law of the appropriate State or Territory, even though the notice does not comply with other requirements of the law of the State or Territory as to the form or content of the notice. For example, the omission from the notice of lien of a description of the property subject to the lien would not affect the validity thereof, even though the law of the State or Territory requires that the notice of lien contain a description of the property subject to the lien. Subsection (b) of this section is declaratory of the existing procedure and in accordance with the long-continued practice of the Treasury Department.

Subsection (c) of this section as redesignated by your committee is in all material respects the same as existing law.

Subsection (d) of this section as redesignated by our committee makes it clear that the Secretary may, after a notice of lien has been filed (and such notice discloses the amount of the outstanding liability as of the time of filing), disclose the extent to which the original obligation has been reduced by subsequent payments.

This is necessary for the protection of persons dealing with property subject to the lien who have a legitimate interest in determining the amount of the outstanding obligation, as well as to aid reestablishment of the taxpayer's credit.

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Supreme Court of the United States

OCTOBER TERM 1957

No. 97

UNITED STATES OF AMERICA,
PETITIONER

VS.

R. F. BALL CONSTRUCTION COMPANY, INC.,
and UNITED PACIFIC INSURANCE COMPANY,
RESPONDENTS

Brief For Respondent, United Pacific Insurance Company

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IN THE

Supreme Court of the United States

No. 97

UNITED STATES OF AMERICA,
PETITIONER

VS.

R. F. BALL CONSTRUCTION COMPANY, INC.,
and UNITED PACIFIC INSURANCE COMPANY,
RESPONDENTS

Brief For Respondent, United Pacific Insurance Company

PRELIMINARY STATEMENT

In a nutshell, the principal question in this case is whether or not prior contract rights may be destroyed by a subsequently filed federal tax lien. Petitioner would have this court overrule its own prior decisions on this question and have this court legislate on matters which Congress has not only failed to legislate upon but has expressly refused to so legislate. A brief, chronological statement of the facts in order to specifically bring before this court the true question involved would seem to be in order.

On July 17, 1951, Ball, a general contractor on a housing project in San Antonio, subcontracted the painting portion of the work to Jacobs and required of him a faithful performance bond. (R.1)

On July 21st, Jacobs applied to respondent surety company for a bond payable to Ball, which was executed by respondent on July 23, 1951. (R.4)

To secure the surety against loss, Jacobs assigned, transferred and conveyed to it "as collateral security for the full performance of the covenants and agreements herein contained and the payment of any other indebtedness or liability of the undersigned to the Company, whether heretofore or hereafter incurred * * * all right, title and interest of the undersigned in and to all percentages retained by the obligee under said contract * * *". (R.5) The retained percentages under this San Antonio contract constitute the basis for this litigation.

Some nine months later, and at a time when Ball had in its hands such of the retained percentages as had been earned up to that time and which had been previously assigned by Jacobs to respondent, Jacobs applied to the respondent for another bond on a contract in Kentucky, which bond was executed by respondent. As part of the consideration for the execution of this bond on April 4 1952, Jacobs agreed to indemnify respondent against all loss, and respondent at that time had the assignment of the retained percentages on the San Antonio housing job as security against loss on the Kentucky job (R.5, 6). Furthermore, at the time the respondent incurred its liability on the Kentucky job, not only had no tax liens been filed, but none of the taxes which are the basis of the petitioner's claim herein were even due. (R.3)

It was stipulated that on April 30, 1953, the Housing Authority in San Antonio accepted the work of Ball, which clearly shows that all work, including the work of Jacobs, was completed, and it was also stipulated that as of April

30, 1953, Ball was indebted to Jacobs in the sum of $13,228.55, as being the retained percentages under this housing contract. (R.2)

Thereafter, notices of tax liens were filed on May 19, 1953, June 9, 1953, and September 5, 1953. (R.3)

There is no stipulation and no evidence in this record as to when Jacobs actually defaulted on the Kentucky job, but between December 1953 and March 1954, respondent surety company "by virtue of its obligation under" the bond which was executed more than a year prior to the filing of any tax liens, and ostensibly with knowledge of the fact that it had as security the retained percentages under the San Antonio housing contract, was required to pay on the Kentucky contract the sum of $12,971.88. (R.6)

While Ball still had in his hands the retained percentages under the housing contract, both petitioner and respondent, along with others no longer of importance, presented claims thereto, so Ball, in order to protect himself, filed this suit in the nature of a bill of interpleader.

BY VIRTUE OF ITS PRIOR ASSIGNMENT THE SURETY BECAME EITHER A "MORTGAGEE, PLEDGEE (OR) PURCHASER" WITHIN THE MEANING OF SEC. 3672 OF THE INTERNAL REVENUE CODE OF 1939.

The assignment in question took place approximately two years prior to the filing of the notice of the Government's tax liens and before the filing of any such notices the amount available as security became fixed and definite in the sum of $13,228.55. Likewise, more than a year before the notice of the Government's tax liens was filed, the surety, ostensibly on the strength of its security, incurred an additional liability on behalf of Jacobs, which obliga-

tion it was later required to discharge in the amount of $12,971.88.

At the time the surety incurred this additional obligation, it had no information that any taxes were due petitioner, and in fact none of the taxes which are the subject matter of this suit were even due at the time the surety entered into its obligation. (R.3)

The courts below, in following all of the decisions up to this time, held that respondent, by virtue of its assignment, attained the status of a mortgagee, pledgee, or purchaser of these retained percentages and as such was protected as against the subsequently filed notices of tax liens under the provisions of section 3672 of the Internal Revenue Code of 1939, now section 6232 of the Internal Revenue Code of 1954, Title 26, U.S.C., which provides in effect that no federal tax lien shall be valid against "any mortgagee, pledgee (or) purchaser" which is prior in time to the filing of notice of such lien. In this holding, we submit that the courts below were correct.

The opinion below speaks eloquently for itself and we will not burden this court with repetition of the arguments and authorities cited therein. There are, however, additional aspects which we desire to bring to the attention of this court.

THE TEXAS LAW WHICH CREATED THE SURETY'S INTEREST PREVAILS

It will be noted that the courts below gave preferred status to the surety as being either a mortgagee, pledgee or purchaser under the Texas law. A subsequent decision confirms the fact that Texas law is controlling on the question of the existence of the surety's interest created by this

assignment. We refer to the case of *Fidelity and Deposit Company vs. N.Y. City Housing Authority*, 241 F.2d 142 (C.A. 2 1957), where the court, in relying upon this court's decision in *Morgan v. Commissioner*, 309 U.S. 78, 80, stated:

> "Section 3670 imposes a tax lien on 'all property and rights to property' of a defaulting taxpayer. In adopting this legislation, the Congress did not create property interests on which a lien might be imposed; there is no suggestion that it authorized the federal courts to do so. On the contrary, it took for granted here, as it normally does in the tax law the vital existence of state laws creating and maintaining various interests. The statute was fashioned to require the courts to determine for federal purposes whether those state-created interests are 'property' or 'rights to property'. That classification of interests is a federal question; the existence of the interests to be federally classified, however, is solely a question of state law.'
>
> "This distinction was formulated by the Supreme Court in Morgan v. Commissioner, 309 U.S. 78, 80, 60 S. Ct. 424, 426, 84 L.Ed. 585, which also involved the tax law. 'State law,' the court explained, 'creates legal interests and rights. The federal revenue acts designate what interests or rights, so created, shall be taxed'."

That this assignment is valid under the Texas law was squarely decided in the case of *Southern Surety Company v. Bering Mfg. Company*, 295 S.W. 337 at 341 where the Texas court said:

> "When Ness as part of the consideration for the execution of the surety bond by the appellant surety company, 'conveyed and assigned unto the said company', as security for indebtedness then due by him to the company and any subsequent indebtedness

> which he might incur to it, 'any and all payments, funds, moneys, and property due, or to become due,' to him under his building contract with the press company, he thereby assigned the fund in question in this case. The validity of the assignment is in no way affected by the fact that there was no fund in actual existence at the time it was made."

The "other indebtedness" clause in this assignment is valid and is a perfectly legitimate contractual business transaction. See *Bridgeton National Bank v. Commercial Cas. Co.*, 180 Atl. 832 (N.J. 1935); *Lacy v. Maryland Cas. Co.*, 32 F.2d 48 (CCA 4, 1929); *Wike v. Board of Trustees*, 49 S.E.2d 740 (N.C. 1948). See also the de facto assignment contained in the 11th section of the bank's charter involved in *Brent v. The Bank of Washington*, 35 U.S. 596, 598. The validity and effect of an assignment of a chose in action "as collateral security" has been recognized by this court in *Conard v. Atlantic Insurance Co.*, 26 U.S. 296, and *Harrison vs. Sterry, 9 U.S.* 286. See also the statement of the Conard case, supra, in *Brent v. The Bank of Washington*, 35 U.S. 596, 612.

The classification of state-created rights in determining what interests are protected under Section 3672, is a matter that involves the intent of Congress. In addition to the discussion of this matter of classification in the opinion of the courts below, we call attention to the enlightening discussion in the unpublished opinion of the trial court in *U.S. v. Gargill*, 218 F.2d 556, wherein the trial court in construing section 3672, said:

> "It seems to me plain that it was the intention of Congress that a mortgage or pledge of any sort should be given priority over an unrecorded tax lien. It makes no difference whether the mortgage

> corresponds to the ancient English form or some other form. It makes no difference whether it is to secure antecedent debt or newly acquired debt. It makes no difference whether the mortgagee is left in possession or not left in possession. The only thing which is required is that the transaction be such that the person or persons claiming to have the mortgage shall have that kind of security which involves either a transfer of title or a lien which is of a nature that gives the holder a right in rem with respect to the property and privilege to precede unsecured creditors. The phrases used in the statute were not used with some medieval notion of mortgage, pledge, or the like. The whole object of the Congressional legislation is not to resurrect a page of Year Book history but to give that protection which persons in a modern world associate with the security that they have achieved as a result of their diligence and forethought."

Surely, the surety in this case obtained by the assignment "that kind of a security which involves either a transfer or title or a lien which is of a nature that gives the holder a right in rem with respect to the property and a privilege to precede unsecured creditors."

As was stated by the courts below:

> "It is the Congress which enacts the law with reference to priorities and not the courts."

And it is the function of this court to determine what Congress had in mind when it used the terms "any mortgagee, pledgee (or) purchaser", in section 3672 of the Internal Revenue Code.

Congress has itself spelled out its intention in connection with the meaning of these words. In 1954 Congress

was in the process of completely revamping the Internal Revenue Code and it had before it the question of whether or not section 3672 of the 1939 Code should be amended. Appendix A of this brief is the complete report of the Committee on Ways and Means in the House of Representatives, and Appendix B hereto is the report of the Committee on Finance of the U. S. Senate having to do solely with amending 3672. It will be noted that in the House report it was suggested that just who is "any mortgagee, pledgee (or) purchaser" should be spelled out, and in explanation of this suggestion the committee report says:

> "This subsection is not designed to extend the protection of subsection (a) of this section to categories of persons now denied protection by existing court decisions (under Section 3672[a] of the 1939 code) which determine who is a mortgagee, pledgee, purchaser, or judgment creditor by reference to the realities and the facts in a given case rather than to the technical form or terminology used to designate such person."

The Senate report rejected the House proposal as being unnecessary and with the subsequent concurrence of the House, Section 3672 was left intact because, as said by the Senate report:

> "Subsection (c) of the House bill provided certain rules with respect to the validity of the tax lien, without the filing of notice thereof, as against mortgagees, pledgees, purchasers, or judgment creditors. The applicable rules have been developed under existing law by judicial construction, and your committee deems it advisable to continue to rely upon judicial interpretation of existing law instead of attempting to prescribe specific statutory rules. The deletion of subsection (c) will continue in effect the existing law.

> "This section corresponds to section 3672 of the 1939 Code. As under existing law, a person who is in fact a mortgagee, pledgee, purchaser, or judgment creditor will be entitled as such to the protection of this section irrespective of the designation applied to such person under State law, for example, in a State which has adopted the Uniform Commercial Code and which uses other terms to describe such persons."

In other words, in 1954 Congress was satisfied with the then court decisions construing the term "any mortgagee, pledgee (or) purchaser" to the effect that regardless of the label placed on a contract lien creditor if he was "in fact a mortgagee, pledgee (or) purchaser" he would be protected and Congress was likewise satisfied with the existing court decisions which determined who is any mortgagee, pledgee (or) purchaser "by reference to the realities of the facts in a given case rather than the technical form or terminology used to designate such persons."

Even the Treasury Regulations themselves spell out this same thing, for Treasury Regulation 301.6323-1 reads as follows:

> "The determination whether a person is a mortgagee, pledgee, purchaser, or judgment creditor, entitled to the protection of section 6323(a), shall be made by reference to the realities and the facts in a given case rather than to the technical form or terminology used to designate such person. Thus, a person who is in fact and in law a mortgagee, pledgee, or purchaser will be entitled as such to the protection of section 6323(a) even though such person is otherwise designated under the law of a State such as the Uniform Commercial Code."

What were these decisions that Congress was satisfied with? They were the very decisions relied on and cited by

the lower courts in this case, such as *Knight v. Knight*, 71 N.Y.Supp. 2d 357, *National Refining Co. v. U.S.*, 160 F.2d 951, *U.S. v. Anders Contracting Co.*, 111 F.Supp. 700, *U.S. v. Gargill*, Supra, *Evans v. Stewart*, 66 NW2d 442 and many others to the same effect.

In its brief the Government argues against according a mortgage status to this assignment. Significantly, the Government verges on destroying its own argument when it recognizes indemnity mortgages in Note 13 of its brief.

THE SURETY WAS AN INDEMNITY MORTGAGEE

The surety, by virtue of the assignment as collateral security, which was executed some two years prior to the filing of any notices of tax liens, became in reality what is known in law as an indemnity mortgagee. Indemnity mortgages have been recognized not only in Texas, but by this court since an early date; an indemnity mortgage being one which is given to secure a surety on its contingent liability. More than 150 years ago, John Marshall, Chief Justice of the United States, in the case of *U.S. v. Hooie*, 3 Cranch 73, 2 L. Ed. 370, upheld an indemnity mortgage as against a claim of priority by the United States. There, one Hooie went surety on a bond for one Fitzgerald and took an indemnity mortgage as security. In a contest of priorities between the United States and the surety, Chief Justice Marshall said:

> "The deed is made to save Hooie harmless on account of his having become security of Fitzgerald to the United States * * *. All the covenants in the deed appear to the court to be fair, legitimate and consistent with common usage."

The court then went on to uphold the mortgage to secure this contingent liability of the surety.

Such was likewise the situation in the very early Texas case of *Williams v. Silliman*, 74 Tex. 626, 12 S.W. 534, where the Supreme Court of Texas upheld an indemnity mortgage to a surety in a very brief opinion, which closed with the statement:

> "The desire to indemnify his security against loss was a sufficient consideration for the execution of the mortgages."

41 Corpus Juris, 459 states as follows:

> "D. INDEMNITY MORTGAGES — 1. VALIDITY IN GENERAL. It is well settled that a mortgage given by way of indemnity, that is, not founded on a present debt, but meant to secure the mortgagee against loss or damage in consequence of a contingent liability or responsibility which he has assumed or agreed to assume for and on behalf of the mortgagor, as surety, bail, indorser, or otherwise, is valid and enforceable.
>
> "FUTURE LIABILITIES. An indemnity mortgage may be given to secure the mortgagee not only as against debts or liabilities for which he has already assumed responsibility or liability, but also to protect him against loss or damage on indorsements, suretyships, or other liabilities which he may in the future enter into for the benefit of mortgagor."

Many authorities from the various states are cited in support of these statements.

The same authority, on page 528, in discussing priorities of an indemnity mortgage, says:

> "A mortgage given to indemnify the mortgagee or to secure him against a secondary or contingent liability, such as that of an indorser or surety, may take precedence over liens created subsequent to its execution * * *"

On this same subject, 36 Am. Jur. 720, has the following to say:

> "A mortgage need not be founded on a present debt, but may be given to secure the performance of other obligations. The mortgage may be made to secure future advances or to indemnify against a contingency which may in fact never occur. It may be given to secure one as an indorser or as a surety upon a bond. The security of a mortgage given to indemnify sureties has been held not to be limited to the nominal money consideration recited, but to extend to the amount for which the sureties ultimately prove liable."

Similar statements are found in 59 C.J.S. 138 and 215.

It is therefore submitted that the surety in this instance was an indemnity mortgagee and when the Congress provided in effect that a federal tax lien would be subordinate to "any mortgagee" which was prior in time, the term "any" included indemnity mortgagees such as the surety in this instance.

THE SURETY COULD BE SAID TO BE PLEDGEE

In regard to a pledgee status, the Government argues that a pledge must be accompanied by a transfer of possession of the property, but the Government fails to point out that the pledgor in question here, namely Jacobs, never had possession. Actual possession was at all times in the prior pledgee who was Ball, the general contractor, and who was holding the retained percentages as security for the performance of Jacob's obligation.

In the case of *Gins v. Mouser Plumbing Supply Co.*, 148 F.2d 974 (CCA 2 1945). The question of the transfer of

possession of pledged property was discussed in a situation similar to that here, namely, where the pledgor is not in possession of the pledged funds or property but such pledged funds or property are in the hands of a prior pledgee. There the court stated:

> "Delivery to the pledgee is required primarily as notice to the pledgor's creditors and possible purchasers that the property in question is no longer free from prior interests of third parties. (citing authorities). But when the property is no longer in the pledgor's possession, ordinarily no good reason exists for requiring further delivery. And the courts have recognized this in holding or indicating with regard to numerous transactions that delivery to or possession by a third party is sufficient to perfect the lender's pledge interest. (citing many authorities)"

Furthermore in the case of *Town of River Junction vs. Maryland Casualty Co.*, 110 F.2d 278, 281 (C.A. 5 1940), cert.den. 310 U.S. 634, the court spoke of retained percentages "just as though the contractor had pledged so many liberty bonds."

As was said by the trial court, relying upon *Knight v. Knight*, supra,

> "It could be said, therefore, as was held in the Knight case, that the bonding company 'comes within the classification of pledgee."

THE SURETY COULD BE SAID TO BE A PURCHASER

The courts below likewise clearly implied that the surety in this case could come within the classification of a purchaser, relying upon *National Refining Co. v. U.S.*, supra. Since the decisions of the lower courts in this case,

the Court of Appeals for the Tenth Circuit has recently handed down its opinion in the case of *Marteney v. U.S.*, 245 F.2d 135.

In that case, Marteney had given his lawyers a note for certain legal services. Subsequently an assignment of interest in a suit that Marteney had against the United Press Association was made to the lawyers in lieu of the note in question. Prior to any final disposition of the suit against the United Press, the Government filed notices of tax liens and after the filing of such notices a judgment was entered in favor of Marteney against United Press for $7500.00, which amount, together with interest, was paid into court. There, as here, the Government contended that its tax lien was superior to the assignment. There the court said:

> "The United States contends that at the time of the agreement Marteney had only an inchoate right which was contingent upon obtaining a judgment, and not transferable. The law of Kansas is that a contingent right in property may be transferred. * * * It was the clear intention of the parties that the attorneys should own the judgment to the extent of the amount due on the note and when Marteney's claim later ripened into a judgment, the transaction was complete. When the judgment was entered, under the terms of the agreement, which Marteney did not repudiate, the attorneys became the owners of Marteney's share of that judgment, or the proceeds thereof, to the extent provided for in the agreement, and to say that they were not purchasers within the meaning of section 3672 would be a failure to acknowledge realities. It would sustain the validity of a secret lien, contrary to the purpose of the statute."

Under the case of *Southern Surety Co. vs. Bering*, Supra, the law of Texas is no different from that of Kansas in that

a contingent right in property may be assigned. The decision in the Marteney case is now final, no appeal to this court having been taken, and, to paraphrase the decision in the Marteney case, "to say that the surety as assignee in this case was not a purchaser within the meaning of 3672, would be a failure to acknowledge realities," and the courts below were correct in indicating that the status of the surety could be classified as that of a purchaser.

THE FACT THAT THE DEBT TO THE SURETY WAS CONTINGENT IS IMMATERIAL

This court, at a very early date, recognized the validity of assignments to secure contingent debts. As heretofore stated, the case of *U.S. v. Hooie*, supra, by this court, upheld the validity of an indemnity mortgage where the debt to be secured was purely contingent. The *Hooie* case is greatly reinforced by the case of *Conard v. Atlantic Insurance Co.*, 26 U.S. 386. In the *Conard* case there was involved a respondentia loan, and in the note appended to the report of that case, (26 U.S. 386) it was said:

> "A *respondentia* loan is a loan of money upon merchandise laden on board a ship, the repayment whereof is made to depend upon the safe arrival of the merchandise at the destined port."
>
> "As the lender sustains the hazard of the voyage, he receives upon its happy termination a greater price or premium for his money than the rate of interest allowed by law in ordinary cases. The premium paid on these occasions depends wholly on the contract of the parties."

In other words, the merchandise in the *Conard* case was assigned to the le der as security for his debt contingent

upon the safe arrival of the vessel. There this court, in classifying this assignment as a mortgage, said (26 U.S. 189 at 213):

> "It is true that in discussions in courts of equity the mortgage is sometimes called a lien for debt and so it certainly is, and something more. It is a transfer of the property itself as security for the debt. This must be admitted to be true at law."

The assignment in the *Conard* case was quite similar to the assignment of the retained percentages in the instant case (See 26 U.S. 446), and of this assignment as collateral security, this court said:

> "But here the transfer was as collateral security. It was therefore a mortgage of the goods and the returns."

There the Government made a similar contention to that made here, namely, that the debt was too contingent to be recognized as valid, but this court struck down such a contention in the following language: (See p. 448)

> "First, it is said that this debt upon a *respondentia* bond is of too contingent a nature to uphold a mortgage, as collateral security for the payment of it. We know of no principle or decision that justifies such a conclusion. Mortgages may as well be given to secure future advances and contingent debts, as those which already exist, and are certain and due. The only question that properly arises in such cases is, the *bona fides* of the transaction. Then, again, it is said that the papers here disclose a transaction fraudulent in its own nature. But we are of opinion that there is no necessary implication of law on the face of these papers, which stamps it fraudulent; for aught that appears, the agreement may have been

> entered into with the most sincere and scrupulous good faith, and whether fraudulent or not, in fact, was a question for the jury upon the whole evidence, which was properly left to their consideration; and they have, by their verdict, negatived the fraud."

So here, if "the only question that properly arises" in this case is "the bona fides of the transaction," there is no hint in the record before this court of any lack of bona fides on the part of either Jacobs or the surety. It was an ordinary business transaction, the like of which takes place every day and obviously the Government did not question in the lower courts the bona fides of the transaction and asked no finding of fact of the trial court relative thereto.

It is therefore submitted that the lower courts were correct in holding that by obtaining an assignment of the retained percentages in question as collateral security the surety in this case came within the protection of section 3672 of the Internal Revenue Code and was either a mortgagee, pledgee or purchaser.

AFTER THE ASSIGNMENT OF THE RETAINED PERCENTAGES TO THE SURETY JACOBS HAD NO PROPERTY OR RIGHTS TO PROPERTY IN SUCH PERCENTAGES SUBJECT TO A SUBSEQUENTLY FILED TAX LIEN.

We believe that in the foregoing section of this brief we have demonstrated that the surety in this instance was entitled to protection by virtue of Section 3672. We submit further, however, that even apart from Sec. 3672 a subsequent federal tax lien is ranked by an antecedent assignment of a chose in action. This court, in *U.S. v. City of New Britain*, 347 U.S. 81, reaffirmed the doctrine of "first in

time is first in right," and this court has held that such antecedent assignment of a chose in action is protected against the impact of the federal priority statute. 31 U.S.C. Sec. 191; *Harrison v. Sterry*, supra, *Conard v. Atlantic Ins. Co.*, supra; and see also *Brent v. The Bank of Washington*, supra. The reasoning in these cases in connection with the priority statute is equally applicable to the tax lien statute. Thus, in *Brent*, supra, in commenting on *Conard*, supra, the court said:

> "It was held in all these cases to amount to a transfer of the absolute right to the property * * *. Such transfer will be protected against the United States though not an out and out sale in the course of business, so as to divest the equitable as well as legal interest of the party."

This divestment of interest of the assignor is fundamental for it means that he has no property in this respect. No property in him necessarily means no property to which the Government's tax lien may attach. There are many cases applying this principle. Leading ones include *Bankers Title & Abstract Co. v. Ferber Co.*, 105 Atl. 2nd 408 (N.J. 1954); *Scott v. Zion Evangelical Lutheran Church*, 70 N.W.2d 326 (S.D. 1955); *Fidelity & Deposit Co. v. N.Y. City Housing Authority*, supra, *Colusa-Glenn Production Assn. v. Phoenix Ins. Co.*, 145 F.Supp. 844 (D.C.Cal. 1956); *Royal Indemnity Co. v. Board of Education*, 137 F.Supp. 890 (D.C., N.C. 1956); *Ala. etc. v. Lehman etc.*, 122 F.Supp. 314 (D.C. Ala. 1954); *U.S. v. Crosland Construction Co.*, 120 F.Supp. 792 (D.C.S.C. 1954); affd. 217 F.2d 275 (C.A. 4. 1954); *Seaboard Surety Co. v. U.S.*, 67 F. Supp. 969 (Ct.Claims 1946) cert. den. 330 U.S. 826, 1947; *U.S. v. Long Island Drug Co.*, 115 F.2d 983 (C.A. 2 1940); *National Iron Bank v. Manning*, 76 F.Supp. 541 (D.C.N.J. 1948).

The no-property concept under the federal tax lien statute has been recognized by this court in *U.S. v. Kaufman*, 267 U.S. 408. Furthermore, this court has recognized that after assignment there is no interest left in the assignor. *Salem Trust Co. v. Mfgrs. Finance Co.*, 264 U.S. 182. The traditional attitude of the courts toward protecting assignments of choses in action is no different today from what it was in the time of Blackstone, for in 2 Blackstone Commentaries, 422, that great commentator stated:

> "* * * and our courts of equity, considering that in a commercial country all personal property must necessarily lie in contract, will protect an assignment of a chose in action, as much as the law will that of a chose in possession."

It is respectfully submitted that the surety in this case is protected by its assignment of the retained percentages as collateral security against a subsequently filed tax lien and that the prior contract right of the surety may not be destroyed by a subsequently filed federal tax lien.

The position of the petitioner in this case is quite similar to that taken by it in the case of *Stewart v. Chinese Chamber of Commerce*, 168 F.2d 708, where petitioner likewise sought to apply property belonging to a non-taxpayer to the payment of taxes owed by a taxpayer. There the court said:

> "The revenue laws are a code or system in regulation of tax assessment and collection. They relate to taxpayers and not to non-taxpayers. The latter are without their scope. No procedure is prescribed for non-taxpayers and no attempt is made to annul any of their rights and remedies in due course of law. With that Congress does not assume to deal and they are neither of the subject nor of the object of the revenue laws.

> "The distinction between persons and things within the scope of the revenue laws and those without them, is vital * * * To the former only does section * * * apply * * * and the well-understood exigencies of government and its revenues and their collection do not serve to extend it to the latter. It is a shield for official action, not a sword for private aggression."

To permit petitioner in this case to take the surety's money to pay the tax liability of Jacobs would be using the revenue laws as "a sword for private aggression." As was said in the case of *Alabama, etc. v. Lehman, etc.*, supra:

> "The assignment in the application for the bond by the principal to the surety has priority over the claim of the United States for taxes which were not due to United States at the time of the assignment."

DISCUSSION OF PETITIONER'S BRIEF

As was pointed out by the courts below, the petitioner is seeking to have this court, as it sought to have the lower courts, judicially amend section 3672, and to change the wording thereof from "any mortgagee" to the words "actual mortgagee" (R. 14) or, as stated by the courts below:

> "The government is seeking to read into section 3672 provisions which Congress has not seen fit to insert therein and the government would have this court construe such section to read: 'such lien shall not be valid as against any mortgagee *whose mortgage is due at a certain time and in a certain amount and which mortgage has been duly recorded in accordance with law.*'
>
> "Had Congress seen fit to make such a requirement it could have done so but I decline to read these words into the statute."

The lower courts further said:

> "The government argues that if an attachment or other judicial lien is not sufficiently 'choate' or complete 'to defeat a subsequent tax lien' then a mortgage to secure future indebtedness should likewise be inferior to a subsequent tax lien. Congress has in fact stated in section 3672 that before an attaching or other similar statutory lienor could claim priority over the government his claim had to ripen into a final judgment. U.S. v. Security Trust etc. supra, U.S. vs. Acri, supra. No such qualification was placed by Congress on the contractual lien of a 'mortgagee.' It is the Congress which enacts the law with reference to priorities and not the courts * * *"

The gist of the Government's contention in this case as it was in the lower courts, is as stated by the lower courts as follows:

> "The Government cites and contends that the case of U.S. v. Security Trust & Savings Bank, 340 U.S. 47, 71 S.Ct. 111; U.S. v. Gilbert Associates, 345 U.S. 361, 73 S.Ct. 701; U.S. v. City of New Britain, 347 U.S. 81, 74 S.Ct. 367; U.S. v. Acri, 348 U.S. 211, 75 S.Ct. 239; U.S. v. Liverpool etc. Ins. Co., 348 U.S. 215, 75 S.Ct. 247; and U.S. v. Scovil, 348 U.S. 218, 75 S.Ct. 244, are in point and are controlling in this case, and says;
>
> > "* * * the principles of United States vs. Security Trust & Sav. Bank; United States v. New Britain; United States v. Scovil; United States v. Acri; and United States v. Liverpool & London Ins. Co. supra, must be applied. "

As was pointed out by the courts below, the decisions of this court in the *Security*, *New Britain*, *Scovil*, *Acri* and

Liverpool cases "dealt with inchoate judgment liens and none of those cases dealt with the contract right of a 'mortgagee', 'pledgee' or 'purchaser'. The latter three categories are all based upon a contract right of some sort, whereas the term 'judgment creditor' and the other liens dealt with in those cases, such as water rent liens, municipal tax liens and landlord's distress liens, arose by virtue of some statutory right, not specifically referred to in section 3672."

As was pointed out by the courts below, the Government made the same contention in the case of *Evans v. Stewart*, supra. In that case the Supreme Court of Iowa said:

> "The only argument the Government advances, that the contract lien is not specific, seems to be that the landlord's contract lien was no different from his statutory lien and under either the landlord had to make his lien specific by taking action to secure possession of the property before either lien would be specific. A short answer to this argument is we are not concerned with the landlord's statutory lien. His contract lien is, we feel, a chattel mortgage and it could hardly be contended that a chattel mortgagee would have to foreclose before he could displace the Government lien under the provisions of Section 3672 making the Government lien invalid as to a mortgagee."

As was further pointed out by the courts below, the distinction between rights created by contract and a statutory lien is made clear by comparing the case of *Evans v. Stewart* with the *Scovil* case, when the lower court said:

> "In the Scovil case, the Supreme Court held that prior to the time it ripened into a final judgment, an incompleted statutory, landlord's lien was inferior to a federal tax lien, since the holder thereof was neither a 'mortgagee', 'pledgee', 'purchaser' nor 'judgment creditor'. In the Evans case the court held

> that a written contract landlord's lien contained in the lease was superior to a federal tax lien because it was a 'mortgage' within 3672. The Government did not appeal the Evans case."

What the petitioner is seeking to do in this case flies directly into the teeth of Mr. Justice Jackson's opinion in the case of *U.S. v. Security Trust & Savings Bank.* There, Justice Jackson goes into the legislative history of Section 3672, and he points out that when this section was adopted in 1939 the Congress itself stated that its intention was to prevent federal tax liens from seriously interfering with "business transactions," which of course meant contract rights. For this court to do what petitioner urges would "seriously interfere with business transactions." Practically no mortgage today is "choate" in the sense that it is a thing complete. In the vast majority of mortgages, pledges or other contract rights, it cannot be determined at the time of the execution thereof how much of the mortgaged or pledged property or funds will have to be used for the payment of the secured debt. In most instances today the mortgagor pays off the debt secured by the mortgage and when this happens there is no need to resort to the pledged or mortgaged fund or property. In other pledges or mortgages the pledgor or mortgagor pays off part of the debt. Furthermore, in most instances, the pledgor or mortgagor has the privilege which it sometimes exercises by paying it in advance, thereby reducing the amount of interest. Furthermore, in most mortgages or pledges, attorneys fees upon default are provided for and, of course, at the time of the execution of the mortgage it cannot be ascertained whether or not attorneys fees will be added to the amount of the mortgaged debt nor how much interest will be due and payable ultimately out of the pledged or mortgaged fund

or property. Therefore, in one sense of the word practically no mortgage today is choate in the sense of being complete in all respects. The business transaction in this case was an open and above-board one and the type of transaction that takes place every day. The whole transaction was in good faith and not intended to defraud creditors, the government or otherwise, and for this court to say that a perfectly legitimate and recognized business transaction such as the one at bar can be disrupted and nullified by a subsequently filed tax lien would "seriously interfere with business transactions" which is the thing that Congress has avidly guarded against.

Shall this court now lay down a rule which would in effect make a mockery of the long accepted Anglo Saxon legal doctrine of freedom of contract and the sanctity of such? Shall it lay down a rule which subverts contract rights acquired prior to the perfection of a tax lien when Congress has specifically refused to do so? Are prior contract rights loaded with a time bomb which can be exploded in the Government's favor when it acquires subsequent tax lien rights? Is the entrepeneur in every prior transaction charged with a notice arising from the statute that rights acquired from a taxpayer can later be divested on behalf of the government? How could business exist under such a rule? "On what meat doth this, our Caesar, feed that he hath grown so great" that he can override long accepted rights and principles?

We feel it safe to say that this court will follow its own decision in the case of Morgan v. Commissioner, supra, wherein it said:

> "State law creates legal interests and rights. The federal revenue acts designate what interests or right, so created, shall be taxed."

The government in this case, however avoids citing decisions from the Texas courts where the right here in question was created. Instead, it cites text writers and goes all over the United States for authorities to support its contentions.

It is clear that under the Texas law as laid down by the Supreme Court in *Williams v. Silliman*, supra; the contract right of the surety in this case was the result of a perfectly legitimate transaction, and the equitable doctrine of relation back has nothing to do with this case.

On page 9 of the petitioner's brief the petitioner says:

> "The courts below concluded that the phrase (other indebtedness) encompassed the indebtedness which subsequently arose between the taxpayer and the bonding company in connection with the entirely independent Kentucky contract. The Government argued that such a construction is erroneous, particularly when considered in light of the fact that a separate bond indemnifying the bonding company was executed in connection with the Kentucky contract (R. 5, 16). See Belton v. Bank, 186 N.C. 614; Wright v. Voorhees, 131 Ia. 408"

For the Government now to state to this court what it argued in the courts below is entirely outside of the record and not only is it outside of the record but it is an incorrect statement as well. The gist of the petitioner's argument in the lower courts was as stated in the lower courts' opinion. The Iowa and North Carolina cases now cited were not submitted either to the trial court or to the Court of Appeals. Both of these cases go off on the intent of the contracting parties, and the trial court in this case was given no opportunity to make a finding of fact as to such intent or as to what was within the contemplation of the parties to the

assignment of the retained percentages as collateral security. If the Iowa law as set forth in *Wright vs. Voorhees*, cited by petitioner, had any bearing on this case at all, which it does not, the Iowa court called attention to its previous decision in *Hellyer v. Briggs*, 55 Ia. 185, 7 N.W. 490, and said with reference to that case:

> "The mortgage was given to secure a general liability of the mortgagee as surety for the mortgagor under a bond and was held to cover all the indebtedness of the mortgagor secured by such bond"

The *Hellyer* case is much more nearly in point here than is the *Wright* case.

On page 15 in footnote 12, the petitioner states:

> "As just pointed out in the text, the after-acquired property here did not come into existence until April 30, 1953. At that very moment, the taxpayer's right to the $13,228.53 became subject to the federal tax lien which had arisen on March 16, 1953."

With this statement we take issue. The subject matter of this lawsuit is the retained percentages under a construction contract that began shortly after July 21, 1951. These percentages were retained by Ball from his payments to Jacobs throughout the time that the construction was in progress and the retained percentages did not "come into existence" on April 30, 1953. They came into existence as the work progressed. It was on April 30th that the work was formally accepted. How long before April 30th Jacobs' work had been completed and all of the retained percentages earned, does not appear in this record. Obviously this time element was not thought to be of any consequence by the petitioner in the trial court; otherwise stipulations

would have been demanded in connection therewith. Furthermore, although, as against Jacobs, possibly March 16, 1953, might be an important date insofar as the attaching of the tax lien is concerned, but the date March 16, 1953, has no bearing whatsoever as to the surety under 3672.

In the same footnote, the petitioner said:

> "Moreover, even a mortgage of after-acquired property requires a debt (or other obligation) as the subject of the mortgage. Here the debt did not arise until the period between December 1953 and March 1954—long after the federal tax liens had been recorded."

With this statement we likewise take issue. The obligation of the surety in this case was incurred when it executed the Kentucky bond on April 4, 1952, a year before any tax liens arose. The terminology of the faithful performance bond on the Kentucky contract is not in this record. However, by going to any form book this court can see the usual terms of such a bond, which terms are as follows:

> "KNOW ALL MEN BY THESE PRESENTS:
>
> That We, as principal and as surety, are held and firmly bound unto as obligee in the sum of $35,59[illegible] (R. 5), for which sum we bind ourselves, our heirs, executors, administrators, successors and assigns, jointly and severally by these presents:
>
> The condition of the above obligation is that: whereas on the 4th day of April, 1952, the principal entered into a contract with the obligee for

> NOW, THEREFORE, if the principal shall faithfully perform said contract according to its terms, covenants and conditions, then this obligation shall be null and void; otherwise to remain in full force and effect."

It is obvious that under such terminology the surety in this instance obligated itself to the extent of nearly $36,000 on the Kentucky contract on April 4, 1952. This obligation was subject to being nullified only if the principal discharged his obligations, which he did not do. For the petitioner now to say that the debt did not arise for a year and a half after the faithful performance bond was executed is sheer sophistry.

Likewise on page 15 in footnote 13, the petitioner says:

> "Although as applied to indemnity mortgages, there is authority (see 1 Jones on Mortgages, supra, Section 467, and cases cited) holding that the lien of such a mortgage takes effect from the time of its execution and delivery (particularly where an obligation to incur future liabilities exists), such authority has no standing in cases involving federal tax liens for, as this Court has said, the doctrine of relation-back has no application in such cases. United States v. Security Tr. & Sav. Bk., 340 U.S. 47, 50."

This court has never made any such statement and has never held that an indemnity mortgagee does not come within the category of "any mortgagee" within the meaning of Section 3672. All that this court said in the *Security Trust* case was that state law which provided that the lien of an attaching creditor upon final judgment related back to the time of the attachment could not affect an intervening federal tax lien. That is a far cry from holding that an

indemnity mortgagee does not fall within the classification of "any mortgagee".

On page 18 of its brief, petitioner says:

> "Moreover, Section 3672 (a) affords no protection, we believe, to mortgages for future advances, but rather only mortgages securing existing debts."

Petitioner then cites regulations of the Internal Revenue Service as authority. There was no need to cite the treasury regulations on the subject of an "open-end" mortgage. The case of *U.S. v. Phillips*, 198 F.2d 634 is ample authority to the effect that where an open-end mortgagee voluntarily pays money to the taxpayer against whom tax liens have already been filed, the Government is prior, but, as pointed out by the courts below, the payment by the surety in this case after the tax liens had been filed was not a voluntary payment at all; it was the discharge of an obligation which it had incurred more than a year prior to the fixing of any tax liens at all.

The petitioner continually refers, particularly on pages 18 and 19, to the payments made by the surety under its contractual obligation as being "advances". Just why petitioner should use the word "advances" in describing the payments made by the surety on an obligation which it assumed long prior to the fixing of any tax liens, is not clear unless it is for the purpose of misleading this court.

Webster defines the word "advance"—"to furnish, as money or other value, before it is due in aid of an enterprise; to supply beforehand." Of course, the surety in this case did not advance any moneys at all. On April 4, 1952, it obligated itself to pay $35,591 and when its principal defaulted it made payment as it was required to do under

its obligation. There is nothing in this transaction at all that could be properly classified as "advances."

The above comments relative to petitioner's brief in this case are merely illustrative of the adroit semantics resorted to by petitioner in this case. Other portions of petitioner's brief fall in the same category, but to point each and all of these out would unduly prolong this brief. The petitioner in this case is seeking to extend to commercial transactions and rights based upon contracts the principle that this court has heretofore applied to mere statutory liens which had not ripened into judgment liens. As was said at the American Bar Association meeting in July of this year in New York by Mr. J. Harry Cross, Esq. of the Baltimore Bar (see Proceedings of the Section of Insurance etc. of the American Bar Association for 1957):

> "As discussed above, the Supreme Court has considered the effect of a federal tax lien upon the interests of others. However, in every instance since the 1950 line of decisions, the interests of others consisted of state statutory liens. There, the court seemed concerned with the proposition that the state cannot by statute impair the standing of federal liens without the consent of Congress. The Supreme Court, having granted the Government's petition for certiorari in the Ball case, will now, for the first time, be confronted with the interest of another consisting of an antecedent contractual right, arising as a part of the transaction by which the chose in action had inception.
>
> "The commercial world will await the outcome with extraordinary interest because the Government's position, if successful, might subordinate a widely used credit arrangement — an assignment of money due or to become due under an existing contract, as collateral security — such subordination being to a federal tax lien against the assignor, which tax

lien was not in existence when the assignment was made, but arose subsequently."

CONCLUSION

It is submitted that Congress has never intended that antecedent contractual rights should be divested by a subsequently filed federal tax lien and that the courts below were correct in so holding, and that therefore the judgment of the courts below should here be affirmed; otherwise this would be a case of "robbing Peter" not to pay Paul, but to pay Caesar.

Respectfully submitted,

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APPENDIX A

EXCERPT FROM REPORT OF THE COMMITTEE ON WAYS AND MEANS, HOUSE OF REPRESENTATIVES, TO ACCOMPANY H.R. 8300—HOUSE REPORT NO. 1337, DATED MARCH 9, 1954. 83rd CONGRESS. UNITED STATES GOVERNMENT PRINTING OFFICE. Page A406

Section 6323. **Validity against mortgagees, pledgees, purchasers, and judgment creditors**

This section corresponds to section 3672 of the 1939 code. Subsection (b) makes it clear that the notice of lien shall be valid, notwithstanding any law of the State or Territory regarding the form or content of a notice of lien, if the notice is in such form as would be valid if filed with the clerk of the United States district court pursuant to subsection (a) (2) of this section. The Treasury Department has consistently taken the position that section 3672 of the 1939 code and the corresponding provisions of prior law authorize the State or Territory only to designate the local office for the filing of the notice of the lien. Subsection (b) is designed to eliminate any question as to the validity of the lien as against mortgagees, pledgees, purchasers, and judgment creditors, where notice thereof is filed in the office designed by the law of the appropriate State or Territory, even though the notice does not comply with other requirements of the law of the State or Territory as to the form or content of the notice. For example, the omission from the notice of lien of a description of the property subject to the lien would not affect the validity thereof, even though the law of the State or Territory requires that the notice of lien contain a description of the property subject to the lien. Subsection (b) of this section is declaratory of

the existing procedure and in accordance with the long-continued practice of the Treasury Department.

Subsection (c) makes it clear that the protection of subsection (a) of this section is not extended to a mortgagee, pledgee, or purchaser who takes with notice or knowledge of the existence of the Federal lien; and that such protection is not extended to a judgment creditor who does not have a valid judgment obtained in a court of record and of competent jurisdiction or to a judgment creditor who does not have a lien which has been properly perfected under such a judgment. This subsection is not designed to extend the protection of subsection (a) of this section to categories of persons now denied protection by existing court decisions (under section 3672 (a) of the 1939 code) which determine who is a mortgagee, pledgee, purchaser, or judgment creditor by reference to the realities and the facts in a given case rather than to the technical form or terminology used to designate such person. Paragraph (1) of subsection (c) provides that the lien shall be valid, without the filing of notice thereof, as against any mortgagee, pledgee or purchaser, if such mortgagee, pledgee, or purchaser had notice of knowledge of the existence of the lien at the time the mortgage, pledge, or purchase, was made. A dual requirement is set forth in paragraphs (2) and (3) of this subsection which a judgment creditor must meet to be entitled to the protection of the notice provisions of subsection (a) of this section. One requirement is that the judgment creditor must have actually obtained a valid judgment in a court of record and of competent jurisdiction for the recovery of specifically designated property or for a certain sum of money; and the other requirement is that the judgment creditor, in the case of a valid judgment for the recovery of a certain sum of money, must have a perfected lien under such judgment on the property as to

which the claims of the contesting parties relate. Furthermore, subsection (c) makes clear that particular persons shall not be treated as judgment creditors because State or Federal law artificially provides or concedes such persons rights or privileges of judgment creditors, or even designates them as such, when they have not actually obtained a judgment in the conventional sense.

Subsection (d) of this section is in all material respects the same as existing law.

Subsection (e) of this section makes it clear that the Secretary may, after a notice of lien has been filed (and such notice discloses the amount of the outstanding liability as of the time of filing), disclose the extent to which the original obligation has been reduced by subsequent payments. This is necessary for the protection of persons dealing with property subject to the lien who have a legitimate interest in determining the amount of the outstanding obligation, as well as to aid reestablishment of the taxpayer's credit.

APPENDIX B

EXCERPT FROM REPORT OF THE COMMITTEE ON FINANCE, UNITED STATES SENATE, TO ACCOMPANY H.R. 8300—UNION CALENDAR NO. 1635, DATED JUNE 18, 1954. 83RD CONGRESS. REPORT NO. 1622, PRINTED IN THE U.S. GOVERNMENT PRINTING OFFICE,

Page 575

Section 6323. **Validity against mortgagees, pledgees, purchasers and judgment creditors**

This section corresponds to that of the House bill except

for the deletion of subsection (c) of the House bill and conforming changes incident to such deletion.

Subsection (c) of the House bill provided certain rules with respect to the validity of the tax lien, without the filing of notice thereof, as against mortgagees, pledgees, purchasers, or judgment creditors. The applicable rules have been developed under existing law by judicial construction, and your committee deems it advisable to continue to rely upon judicial interpretation of existing law instead of attempting to prescribe specific statutory rules. The deletion of subsection (c) will continue in effect the existing law.

This section corresponds to section 3672 of the 1939 Code. As under existing law, a person who is in fact a mortgagee, pledgee, purchaser, or judgment creditor will be entitled as such to the protection of this section irrespective of the designation applied to such person under State law, for example, in a State which has adopted the Uniform Commercial Code and which uses other terms to describe such persons.

Subsection (b) of this section makes it clear that the notice of lien shall be valid, notwithstanding any law of the State or Territory regarding the form or content of a notice of lien, if the notice is in such form as would be valid if filed with the clerk of the United States district court pursuant to subsection (a) (2) of this section. The Treasury Department has consistently taken the position that section 3672 of the 1939 Code and the corresponding provisions of prior law authorize the State or Territory only to designate the local office for the filing of the notice of the lien. Subsection (b) is designed to eliminate any question as to the validity of the lien as against mortgagees, pledgees, purchasers, and judgment creditors, where notice thereof is filed

in the office designated by the law of the appropriate State or Territory, even though the notice does not comply with other requirements of the law of the State or Territory as to the form or content of the notice. For example, the omission from the notice of lien of a description of the property subject to the lien would not affect the validity thereof, even though the law of the State or Territory requires that the notice of lien contain a description of the property subject to the lien. Subsection (b) of this section is declaratory of the existing procedure and in accordance with the long-continued practice of the Treasury Department.

Subsection (c) of this section as redesignated by your committee is in all material respects the same as existing law.

Subsection (d) of this section as redesignated by our committee makes it clear that the Secretary may, after a notice of lien has been filed (and such notice discloses the amount of the outstanding liability as of the time of filing), disclose the extent to which the original obligation has been reduced by subsequent payments. This is necessary for the protection of persons dealing with property subject to the lien who have a legitimate interest in determining the amount of the outstanding obligation, as well as to aid reestablishment of the taxpayer's credit.

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NO. 97

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1957

UNITED STATES OF AMERICA, PETITIONER

v.

R. F. BALL CONSTRUCTION COMPANY, INC.
and UNITED PACIFIC INSURANCE COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR APPELLEE-INTERPLEADER R. F. BALL CONSTRUCTION COMPANY, INC.

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COMMERCIAL RECORDER, FORT WORTH, TEXAS— 10-31-57—40

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BRIEF FOR APPELLEE-INTERPLEADER R. F. BALL CONSTRUCTION COMPANY, INC.

STATEMENT

The Government, Appellant, takes the position that if it prevails over United Pacific Insurance Company

and establishes a prior right to the fund, this Court should deny to Appellee-Interpleader the $500.00 fee which was ordered paid out of such fund.

The stipulation which the Government, as a party Defendant to the immediate interpleader suit, entered into is as follows:

> "11. This case originated in the State District Court of Bexar County, plaintiff therein filing a suit in the nature of a Bill of Interpleader, and tendering into court the $13,228.55. The allegations of plaintiff's petition with reference to the dispute over such fund and with reference to its inability to make payment thereof without subjecting itself to possible double liability, are true. Plaintiff asks allowance of interpleader fee and its court costs, to be payable out of the $13,228.55. It is stipulated that a reasonable fee for the services performed by Simon & Simon, attorneys for R. F. Ball Construction Co., Inc. (the interpleader) is $500; provided a fee may be allowed by the Court to the interpleader's attorneys out of the $13,228.55 in question, under applicable principles of law." (TR. 4)

ARGUMENT

In support for this position, the Government relies entirely on certain language in *U. S.* vs. *Liverpool and London and Globe Insurance Company*, 248 U. S., 215. Said decision is not applicable to the present case for each and all of the following reasons:

a. *Liverpool* was a garnishment suit and the costs and garnishee fee were adjudged by your Honors in accordance with Texas Rule 677. Texas Rule 677 relating to costs in garnishment cases provides "where the garnishee is discharged upon his answer, the costs of the proceeding including a reasonable compensation to the garnishee, shall be taxed against the plaintiff; where the answer of the garnishee has not been controverted and the garnishee is held thereon, such costs shall be taxed against the defendant and included in the execution provided for in this section;**"

The plaintiff in a garnishment suit assumes the risk of the payment of costs, including the garnishee fee, in the event that he catches no funds or properties in garnishee's hands and the garnishee is discharged. If funds are caught, the defendant (meaning the defendant in the main action) must pay all costs including garnishment costs and garnishee fee. Your Honors, in *Liverpool*, adjudged the costs in accordance with the Texas Garnishment Rule of Procedure. There is no similar statutory provision in Texas for taxing of costs in an interpleader action. In both State and Federal courts, interpleader costs are usually paid out of the fund, pursuant to long-established equitable principles.

The stakeholder has no interest in the fund which he holds, and can neither win nor lose by the court proceeding. Hence, inasmuch as he cannot pay the money to one contesting party without running the hazard of liability to the other, courts have long recog-

nized the interpleader process by which the stakeholder deposits the funds in the registry of the court. If he is a valid interpleader, then his costs and fees are paid out of the impounded fund. It would seem unfair to tax interpleader fees against the loser of the contest over the funds.

If the Government position is sustained, interpleader will be deprived of its costs and fee, unless the same are adjudged against United Pacific. This situation points up the difference between a garnishment action, wherein the initiating plaintiff guarantees garnishee fee in event that he fails to catch funds or property in the hands of the garnishee, and the interpleader action, which is instituted by a stakeholder, who looks to the fund for compensation of fees and costs.

Liverpool was decided under garnishment statutes (Rules) as to costs. The decision is not applicable to interpleader.

b. In *Liverpool*, the Government refused to consent to being joined as an adverse party, and garnishee's complaint against it was dismissed. The Government then intervened in the case in order to preserve its position as a plaintiff. Similarly in *Ford Motor* vs. *Hackert*, *143 F. S. 216*, the Government withheld consent to the interpleader and was dismissed, and then filed intervention asserting that its tax lien was paramount. Also in the Ford Motor case the court held that the plaintiff was not sufficiently disinterested to be deemed a true interpleader. In our

immediate case the Government not only consented to the interpleader suit and remained therein as a defendant, but the Government stipulated that plaintiff's petition with reference to the existence of a dispute and with reference to its possible double liability were true. (Tr. 4). Having elected to seek its recovery through this interpleader suit, the Government cannot avoid usual and normal incidents thereof, which include the deduction of the fee prior to distribution of balance to the winning party.

The situation is not unlike *In Re Boyer, 130 F. S. 20* where the Government sustained its lien in a bankruptcy proceeding, but the court ruled that the fees of the trustee and referee were payable out of the proceeds of sale.

c. As discussed in *U. S.* vs. *Ullman, 115 F. S. 211,* there is no reason why the general rules of interpleader become inapplicable where the Government is one of the contending parties. The Ullman argument is discussed and upheld in a recent case by the St. Louis Court of Appeals, *American Alliance Insurance Company* vs. *Mitchell, 299 S. W. 2d 536.*

Federal Courts have recognized the general principles governing interpleader procedures:

Massachusetts Mutual Life Insurance Co. vs. *Morris,* 61 F. 2d 104;

New York Life Insurance Co. vs. *Miller*, 139 F. 2d 657;

Globe Indemnity Co. vs. *Puget Sound*, 154 F. 2d 248;

Palomas Land & Cattle Co. vs. *Baldwin*, 189 F. 2d, 946.

In our immediate case we have the further situation of the Government stipulating for the payment of the reasonable fee of $500.00 provided that the same may be allowed out of the fund "under applicable principles of law." (Tr. 4).

The Government has suggested no reason why these applicable principles, governing interpleaders generally, should not apply here.

We have found no reference to the Liverpool case in Bruce vs. U. S. cited by the Government, nor can we find any pertinency. In the Boston Insurance case, the Government was invited to intervene. The judgment of the court was based on the Liverpool decision, without any discussion thereof.

CONCLUSION

WHEREFORE, Appellee-Interpleader prays that the decree of the United States Court of Appeals for the Fifth Circuit be affirmed insofar as such decree

approves payment of its interpleader expenses, and for general relief.

Attorney for Appellee-
Interpleader, R. F. Ball
Construction Company, Inc.

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FILED
MAR 27 1958
JOHN T. FEY, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1957

No. 97

UNITED STATES OF AMERICA,
PETITIONER

VS.

R. F. BALL CONSTRUCTION COMPANY, INC.,
and UNITED PACIFIC INSURANCE COMPANY,
RESPONDENTS

Petition for Rehearing

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TO THE SUPREME COURT OF THE UNITED STATES:

Comes now the respondent United Pacific Insurance Company and petitions this court for a rehearing and prays that this court upon such rehearing affirm the judgments of the lower courts, and as grounds therefor this respondent would show to the court as follows:

When the representative of the Attorney General's office argued this case in the trial court, he in effect threatened the trial court by stating that if he did not decide this case in favor of the Government, the case would be appealed to the Supreme Court of the United States (no mention was made of the Court of Appeals), and it was further implied that the Supreme Court would reverse this case in favor of the Government because the Supreme Court did not decide cases against the United States Government. The Attorney

General's office apparently has now made good on this threat, because a bare majority of five members of this court, in a per curiam opinion, has reversed the judgments of the trial court and the Court of Appeals and decided this case in favor of the United States Government.

> "Traditionally, it may be pointed out that a 'per curiam' is the opinion of the court in which the judges are all of one mind and the question involved is so clear that it is not considered necessary to elaborate it by an extended discussion" *Newmans v. Lakeworth Drainage District* (S.Ct.Fla., 1956) 87 So. 2d 49.

See also 32 Words and Phrases 17, and cases cited thereunder, and 14 American Jurisprudence, 37.

We realize that the majority of this court, as presently constituted, has no hesitancy in breaking with tradition, and it has the power to re-define terms and even coin new words, such as the word "choate". See 42 American Bar Journal 608, July 1956. But we ask this court, in all sincerity, does it have the right, as distinguished from having the power, to "per curiam" this case when eight judges of the United States courts (one trial judge, three Appeals Court judges and four Supreme Court judges) have said that the two cases cited by the majority of this court as supporting its action, have nothing whatsoever to do with this case?

What is the question that is involved in this case? The trial court and the Court of Appeals stated the question to be as follows:

> "The principal question for determination by this court is as to which lien is prior—the Government's tax lien which arose by virtue of the filing of the notice of its tax liens in May, June and September

> of 1953, or the contract lien of the Bonding Company which arose long prior thereto by virtue of the assignment of the retained percentages in question by Jacobs to the Bonding Company which by contract protected the Bonding Company from the loss which it incurred on the Louisville job which became a potential loss upon the execution of the Louisville bond on April 4, 1952, prior to the filing of the Government's tax liens but which was not paid under its bond until after the filing of the Government's tax liens."

The dissenting opinion in this case states the question as being as follows:

> "The question presented is whether an 'assignment' made by a subcontractor to his performance-bond surety of all sums to become due for performance of the subcontract, as security for any indebtedness or liability thereafter incurred by the subcontractor to the surety, constituted the surety a 'mortgagee' of those sums within the meaning of sec. 3672(a) of the Internal Revenue Code of 1939, as amended."

We submit that the above are correct statements of the question that is involved in this case. Now let us see what the question was in the Security Trust Company case. As stated by this court in its opinion in the case of *United States v. Security Trust and Savings Bank*, 340 U.S. 47:

> "The question presented here is whether a tax lien of the United States is prior in right to an attachment lien where the federal tax lien was recorded subsequent to the date of the attachment lien but prior to the date the attaching creditor obtained judgment."

And what was the question in the New Britain case?* This court stated the question very succinctly in its opinion in *United States v. City of New Britain*, 347 U.S. 81, wherein it said:

> "The question presented by this writ involves the relative priority of statutory federal and municipal liens to the proceeds of a mortgage foreclosure sale of the property to which the liens attached."

It is submitted that the questions involved in the *Security Trust* and *New Britain* cases did not even remotely involve the question that is involved in this case, and eight Federal judges have so held, but this court merely "per curiamed."

It will be noted that in the courts below it was stated:

> "The government argues that if an attachment or other judicial lien is not sufficiently 'choate' or complete 'to defeat a subsequent tax lien' then a mortgage to secure future indebtedness would likewise be inferior to a subsequent tax lien. Congress has in effect stated in Sec. 3672 that before an attaching or other similar statutory lienor can claim priority over the government his claim had to ripen into a final judgment. U. S. v. Security Trust, supra, U. S. v. Acri, supra. No such qualification was placed by Congress on the contractual lien of a 'mortgagee'. It is the Congress which enacts the law with reference to priorities and not the courts * * *."

We submit that the lower courts were correct in this statement and that this court has now judicially legislated

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*Upon oral argument of this case, Justice Frankfurter stated from the bench that he had never liked the decision in the New Britain case. It was therefore a disappointing surprise to see that Justice Frankfurter not only reaffirmed *New Britain*, which he disliked, but by his vote alone has now extended the principle of *New Britain* far beyond its previous scope and has made this principle apply to an ordinary business contract transaction.

into Section 3672 words which Congress not only did not include, but specifically refused to include. For, as stated by the lower courts:

> "* * * the Government is seeking to read into Section 3672 provisions which Congress has not seen fit to insert therein and the Government would have this court construe such section to read:
>
> > 'Such lien shall not be valid as against any mortgagee *whose mortgage is due at a certain time and in a certain amount and which mortgage has been duly recorded in accordance with law.*'
>
> Had Congress seen fit to make such a requirement it could have done so, but I decline to read these words into the statute."

The majority of this court seems to have no hesitancy in reading into the statute these words which Congress specifically declined to write into it when it amended Sec. 3672 in 1954. Does this not lend support to the conclusion stated by Judge Learned Hand in his recent lectures to the Harvard School of Law, that the majority of this court has, by a "*coup de main*" assumed the role of "a third legislative chamber"?*

We predict that Congress will not allow this judicial legislation to stand and will legislatively overrule this court's decision in this case, as it did this court's decision in *United States vs. Wunderlich*, 342 U.S. 98, and just as it did this court's decision in a somewhat kindred matter in the case of *Corn Exchange National Bank v. Klauder*, 318 U.S. 434, because, as Justice Jackson pointed out in *Security Trust*, supra, Congress has assiduously sought to prevent subsequently filed tax liens from serious interfer-

*The Bill of Rights page 55. Learned Hand. Harvard University Press 1958

ing with prior business transactions, but this will do the litigants in this case no good, nor those similarly situated, until Congress can act.

And what is the effect of this court's per curiam opinion which permits a subsequently fixed federal tax lien to displace a prior contract mortgage? As stated on page 30 of this respondent's brief in quoting from an address to the American Bar Association:

> "The commercial world will await the outcome [of this case] with extraordinary interest because the government's position, if successful, might subordinate a widely used credit arrangement — an assignment of money due or to become due under an existing contract as collateral security — such subordination being to a federal tax lien against the assignor, which tax lien was not in existence when the assignment was made but arose subsequently."

It is submitted that if this court intended to do the above it should do so in no uncertain terms and not leave the matter floating in orbit, as it has so done by giving this case the "per curiam" treatment. Already the Court of Appeals for the Fifth Circuit has called for re-argument in its Cause No. 16,723, *Commercial Standard Insurance Co. v. Campbell, et al*, as to what is the "effect" of the majority decision in this case, and the writer of this brief has received letters from all over the country asking his opinion as to what this court meant by its per curiam, but no one can tell with any degree of certainty just what the effect of this court's decision is.

WHEREFORE, this respondent prays that this court retract its per curiam opinion and adopt the dissenting opinion as the opinion of the court and affirm the judgments of the lower courts.

In the alternative, this respondent prays that at least this court write an opinion which will define the terms "inchoate" and "unperfected," so that this respondent and the business world generally may know how to prepare instruments which will pass the test of this court as to inchoateness and perfection and this court is asked to set forth in an opinion just what tests it prescribes, otherwise the decision of the court in this case will "seriously interfere with business transactions."

Respectfully submitted,

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